Supreme Court, U.S.
FILED

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No. 02-

IN THE

Supreme Court of the United States

ENTERGY LOUISIANA, INC.,

Petitioner,

v.

LOUISIANA PUBLIC SERVICE COMMISSION, *et al.*,

Respondents.

Petition for a Writ of Certiorari to the Supreme Court of Louisiana

PETITION FOR A WRIT OF CERTIORARI

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August 22, 2002

WILSON-EPES PRINTING CO., INC. – (202) 789-0096 – WASHINGTON, D. C. 20001

209 pp

QUESTION PRESENTED

Whether *Mississippi Power & Light* v. *Mississippi ex rel. Moore*, 487 U.S. 354 (1988), and *Nantahala Power & Light Co.* v. *Thornburg*, 476 U.S. 953 (1986), require a state public utility commission to allow an electric utility member of a multi-state power system to recover, in retail rates, the costs allocated to it by a rate schedule of the Federal Energy Regulatory Commission ("FERC"), or whether the state commission has jurisdiction to decide that it was "imprudent" for such a utility to incur the costs allocated to it under a FERC rate schedule, thereby "trapping" such wholesale costs?

PARTIES TO THE PROCEEDING

In addition to the parties listed in the caption, the five Commissioners of the Louisiana Power Service Commision – Hon. C. Dale Sittig, the Hon. Jack "Jay" A. Blossman, Jr., the Hon. Irma Muse Dixon, the Hon. James M. Field, and the Hon. Don Owen – are Respondents in this proceeding and were Defendants below solely in their official capacities as members of the Commission.

Pursuant to Sup. Ct. R. 29.6, Petitioner Entergy Louisiana, Inc. is a wholly-owned subsidiary of Entergy Corporation. Entergy Corporation has no parent company. Old Mutual, the parent company of Barrow, Hanley, Mewhinney & Strauss, owns 11% of the stock of Entergy Corporation. Old Mutual is publicly traded on the London and Johannesburg stock exchanges.

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PETITION FOR WRIT OF CERTIORARI TO THE SUPREME COURT OF LOUISIANA

Entergy Louisiana, Inc. ("ELI") respectfully submits this petition for writ of certiorari to the Louisiana Supreme Court.

OPINIONS BELOW

The opinion of the Louisiana Supreme Court (Appendix ("App.") 1a-21a) is reported at 815 So. 2d 27 (La. 2002). The order of the Louisiana Supreme Court denying the petition for rehearing (App. 159a) is not reported. The opinion of the Nineteenth Judicial District Court for the Parish of East Baton Rouge (App. 22a-23a) is not reported. The order of the Louisiana Public Service Commission (App. 24a-84a), Order No. U-20925-G, is not reported, but is available at 1998 WL 1285300.

JURISDICTION

The opinion and judgment of the Louisiana Supreme Court were entered on April 3, 2002. App. 1a. On May 24, 2002, the Court denied petitioner's timely petition for rehearing. App. 159a. This Court's jurisdiction is invoked pursuant to 28 U.S.C. § 1257.

CONSTITUTIONAL AND STATUTORY PROVISIONS

The pertinent provisions of the Federal Constitution and the Federal Power Act, 16 U.S.C. §§ 791a-828c, are reprinted at App. 165a-175a.

STATEMENT OF THE CASE

In this case, a divided Louisiana Supreme Court affirmed a decision by the Louisiana Public Service Commission ("LPSC") barring a local electric utility (ELI) from

recovering in retail rates – and thus "trapping" – costs that ELI was required to incur under a Federal Energy Regulatory Commission ("FERC") rate schedule. By unlawfully determining the "prudence" of ELI's compliance with a FERC-approved rate schedule, the state court and the LPSC are exercising jurisdiction that Congress assigned exclusively to FERC. The LPSC took these actions after FERC denied the complaint it previously had filed challenging the very allocation of costs in issue and after the D.C. Circuit affirmed that FERC decision.

The Louisiana Supreme Court decision is thus squarely contrary to *Mississippi Power & Light Co.* v. *Mississippi ex rel. Moore*, 487 U.S. 354 (1988) ("*MP&L*") and *Nantahala Power & Light Co.* v. *Thornburg*, 476 U.S. 953 (1986) ("*Nantahala*"). It is similarly contrary to the decisions of numerous state supreme courts and to decisions of the federal courts of appeals for the District of Columbia, First, Fourth, and Eighth Circuits. The only decision that provides any support for the Louisiana Supreme Court's judgment is an earlier decision of the Fifth Circuit that this Court granted certiorari to review, but that was dismissed when the parties settled the case. *New Orleans Pub. Serv., Inc.* v. *Council of the City of New Orleans*, 911 F.2d 993 (5th Cir. 1990), *cert. dismissed*, 502 U.S. 937 (1991) ("*NOPSI*"). Both the decision below and the *NOPSI* decision are in clear and irreconcilable conflict with this Court's decisions. Yet those decisions have twice been misunderstood and misapplied. This Court's review is warranted to resolve the conflict.

Such review is important because the decision below not only undermines the integrity of the System Agreement governing an electric system providing service in Arkansas, Louisiana, Mississippi, and Texas, but also undermines the Congressional scheme for regulation of interstate power. The Federal Power Act directs FERC to "promote and encourage" "voluntary interconnection and coordination of facilities for the generation, transmission, and sale of electric energy" in

the interest of "assuring an abundant supply of electric energy throughout the United States with the greatest possible economy." 16 U.S.C. § 824a(a). Congress gave FERC this jurisdiction precisely to prevent parochial local interests from impeding the achievement of benefits available through the coordinated operations of multi-state electric systems. This Congressional scheme will be substantially undermined if states may review for themselves the prudence of costs and benefits allocated by FERC pursuant to multi-state agreements and bar recovery of FERC-allocated costs. The need for review here is heightened by the strategy employed by the LPSC, and evidenced in this case, of using its own proceedings to subvert FERC's jurisdiction in order to serve its own interests. In view of the ruling below and *NOPSI*, a decision from this Court on this issue is the only certain means of preventing Louisiana and other state utility commissions from creating the disruptions of interstate commerce that the Federal Power Act was enacted to prevent.

1. The Multi-state Entergy System and FERC Rate Schedules. This case arises in the same "integrated power pool" involved in *MP&L*, 487 U.S. at 357, and *NOPSI*.[1] Petitioner ELI is an electric public utility that operates in Louisiana. It is a subsidiary of, and wholly owned by, a public utility holding company, Entergy Corporation. Entergy also owns four other utility operating companies, Entergy Arkansas, Inc., Entergy Gulf States, Inc., Entergy Mississippi, Inc., and Entergy New Orleans, Inc. "The five operating companies plan, construct, and operate their collective electric generating and transmission facilities as a single, integrated system serving parts of Louisiana, Arkansas, Mississippi, and Texas." App. 3a.

The current Entergy System Agreement, adopted in 1982 and subsequently amended, governs arrangements among the

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[1] Entergy Corporation was formerly Middle South Utilities, Inc. App. 4a n.3.

operating companies for the transmission, sale, and exchange of energy. Its purpose is:

> "to provide the contractual basis for the continued planning, construction, and operation of the electric generation, transmission and other facilities of the [operating companies] [and to] provide[] a basis for equalizing among the companies any imbalance of costs associated with the construction, ownership and operation of such facilities as are used for the mutual benefit of all the [operating companies]." [App. 3a-4a.]

The System Agreement is administered by a system-wide operating committee, the Entergy Operating Committee. The System Agreement is a rate schedule filed with and approved by FERC; any changes to the Agreement must be approved by FERC. See *Louisiana Pub. Serv. Comm'n.* v. *FERC*, 174 F.3d 218 (D.C. Cir. 1999) ("*LPSC*").

The System Agreement includes rate schedules that allocate resources and associated costs among the five operating companies and that are known as Service Schedules. These schedules are "formula" rate schedules in that they do not specify particular rates or cost allocations. Rather, they set forth formulas that prescribe how the allocations are to be calculated or determined and that delegate the application of certain aspects of the formula to the Entergy Operating Committee, subject to review by FERC in the event of claims that the formula had been misapplied. Once a Service Schedule is approved by FERC, it becomes part of the System Agreement.

One such service schedule – Schedule MSS-1, Reserve Equalization – is the subject of this case.[2] MSS-1 establishes a mechanism for equalizing generating reserves among the

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[2] "MSS" refers to the former name of the System's service company, Middle South Services, Inc. The number "1" indicates only that this is one of several Service Schedules. App. 4a n.3.

operating companies. Under MSS-1, each operating company bears responsibility for a share of the total Entergy system capability; that share is a function of the company's contribution to the System's peak load. Companies providing less than their calculated share of the System's capability make payments to companies providing more than their share. "Each of the operating companies makes or receives payments based on whether its capacity exceeds, equals, or is less than the system capability for which it is responsible." App. 5a. See also *LPSC*, 174 F.3d at 220 (characterizing MSS-1 as "the inter-company formula tariff that [FERC] administers to equalize costs among [the five Entergy operating companies]").

A generating unit must be "available" for use by the System, as defined in Section 10.02 of the System Agreement, in order to be counted as part of an operating company's capability in the calculation of MSS-1 payments.

During the mid-1980's, the Entergy operating companies had excess generating capacity. They implemented the Extended Reserve Shutdown ("ERS") Program, "to save money (for the customers, as well as for the companies themselves) by placing the excess generating units in an inactive, *i.e.*, extended reserve status." App. 6a. The System kept 24 units in ERS status in order to retain the capability to meet any future increase in power demand, yet "were able to reduce operating staff and maintenance costs and defer costs of repairing the units." *Id.*

The Entergy Operating Committee decided that units in ERS status should be considered "available" for purposes of calculating individual operating companies' capacity under MSS-1. As a result, ELI made higher MSS-1 payments than it would have made if none of the ERS units had been included in the MSS-1 computation.

2. The FERC ERS Proceedings. In 1993, FERC reviewed the System Agreement and initiated proceedings to

determine, inter alia, whether Entergy had violated the Agreement by including the ERS units in the MSS-1 computations. The LPSC intervened in that FERC proceeding, filing a separate complaint alleging that Entergy had violated the System Agreement by treating the ERS units as "available" capacity and seeking retroactive refunds for ELI's LPSC-jurisdictional customers, plus accrued interest.

A FERC Administrative Law Judge ("ALJ") concluded that, although the end result was just, reasonable, and not unduly discriminatory, the ERS units were not "available" for purposes of MSS-1 calculations within the meaning of Section 10.02 of the System Agreement, as then defined,[3] and therefore concluded that Entergy had violated the System Agreement. He rejected, however, the LPSC's request for refunds based on several considerations, including the substantial savings for ratepayers generated by the ERS program and his conclusion that the end result was just, reasonable, and nondiscriminatory. He also determined that the System Agreement should be amended going forward to allow ERS program units to be deemed "available" in the future. App. 124a-125a, 139a-140a, 151a-152a.

FERC affirmed that decision, including the ALJ's rejection of the LPSC's request for a refund of alleged overpayments. In so doing, FERC explained that Entergy's ERS program had provided significant benefits and overall cost-savings for the

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[3] Prior to August 5, 1997, section 10.02 of the System Agreement provided in pertinent part:

> "A unit is considered available to the extent the capability can be demonstrated and (1) is under the control of the System Operator, or (2) is down for maintenance or nuclear refueling. A unit is considered unavailable if in the judgment of the Operating Committee it is of insufficient value in supplying system loads because of (1) obsolescence, (2) physical condition, (3) reliability, (4) operating cost, (5) start-up time required, or (6) lack of due diligence in effecting repairs or nuclear refueling in the event of a scheduled or unscheduled outage." [App. 112a.]

system and that it was "just" and "reasonable" for Entergy to include ERS units in the MSS-1 calculation:

> By including ERS units in the Schedule MSS-1 computation, Entergy continued the previously-approved equalization approach that was established for excess capacity on the Entergy System. Moreover, if Entergy had not undertaken to reduce costs for its system by implementing the ERS program, these units would have been eligible for inclusion in Schedule MSS-1. *We do not believe that the Operating Companies should lose the right to have their costs equalized when they take advantage of the ERS program which, we note, provides very significant benefits for the Entergy system.*
>
> . . . .
>
> . . . By exercising our discretion not to order refunds, we are simply acting consistent with the equities in this case. Indeed, the record evidence demonstrates that, although Entergy acted in a manner inconsistent with Schedule MSS-1, *the end result was just, reasonable, and not unduly discriminatory*. App. 102a-103a (emphases supplied) (footnotes omitted).]

FERC therefore approved a proposed amendment to the System Agreement, effective August 5, 1997, which authorized the Entergy Operating Committee to consider ERS units "available" in MSS-1 calculations if the "'intent of [the Operating Committee is to] return[] the unit to service at a future date in order to meet Entergy System requirements.'" App. 104a (emphasis omitted). FERC further required that the:

> "Operating Committee's decision to consider an ERS unit to be available to meet future System requirements shall be evidenced in the minutes of the Operating Committee and shall be based on consideration of current and future resource needs, the projected length of time the unit would be in ERS status, the projected cost

> of maintaining such unit, and the projected cost of returning the unit to service." [*Id.* (emphasis omitted)].

In making this decision, FERC rejected both the argument of the LPSC that refunds should be allowed for past periods and the argument of the LPSC that the ERS units should be excluded from MSS-1 payment calculations in the future. FERC also denied the LPSC's request for rehearing. App. 160a-164a.

The LPSC pursued its arguments on appeal, but its contentions were rejected by the Court of Appeals for the D.C. Circuit. See *LPSC*, 174 F.3d at 231. In addition to holding that FERC's denial of refunds was lawful, the court of appeals rejected the LPSC's challenge to the amendment to Section 10.02, authorizing inclusion of ERS units in MSS-1 calculations if the Operating Committee intends to return the units to service in the future. The court of appeals held that the amendment was just and reasonable and, if necessary, that "discriminatory implementation of the amendment could be remedied in a proceeding under [Federal Power Act] § 206, 16 U.S.C. § 824e." *Id.*

Following FERC's amendment of the System Agreement, the Operating Committee determined that the ERS units should be considered "available" within the meaning of the amended definition. Based on the presentation of the Director of Resource Planning for Entergy, the Committee concluded that the ERS units were "available" within the meaning of that amendment. Neither the LPSC nor any other party challenged this determination before FERC. Therefore, after August 5, 1997, the ERS units were included in the MSS-1 calculations pursuant to the amended MSS-1 that had been approved by FERC. The reasonableness of this determination was verified by subsequent events for it is undisputed that, consistent with the Operating Committee's assessment, "[b]y 1999, all of the ERS units, with the exception of one, had either been returned to active service, or w[ere] scheduled for return to service." App. 6a n.4.

3. The LPSC Proceedings. During all relevant times, ELI annually filed with the LPSC financial data for the previous year relating to its cost of providing service. The LPSC uses these data to adjust ELI's retail rates. ELI's 1997 filing was based upon data from 1996 and included its MSS-1 payments made during 1996. All of the generating units in ERS status were treated as "available."

The LPSC ordered ELI to remove from its calculations "all MSS-1 overpayments incurred on or after August 6, 1997" that resulted from the inclusion of the ERS units in the MSS-1 calculation. App. 83a. It further ordered ELI to credit the overpayments "back to the ratepayers." *Id.*

The LPSC concluded that Entergy's treatment of ERS units benefited Entergy Arkansas (formerly Arkansas Power & Light Company) and Entergy New Orleans (formerly New Orleans Public Service, Inc.) and penalized ELI and Entergy Mississippi (formerly Mississippi Power & Light Company). The LPSC recognized that under the filed-rate doctrine, state regulators may not challenge FERC-approved wholesale rates and "trap" wholesale costs incurred by a utility. Nonetheless, the LPSC held that the *Pike County* exception applied in this case. Under that exception, a state may review the prudence of a utility's decision to purchase power at a FERC-approved rate if and only if the utility has the right to refuse to purchase that power. *MP&L*, 487 U.S. at 373-74; *Nanatahala*, 476 U.S. at 972 (discussing *Pike County Light & Power Co.* v. *Pennsylvania Public Utility Comm'n*, 465 A.2d 735, 737-38 (Pa. 1983)). The LPSC stated that:

> though FERC has exclusive jurisdiction over the issue of whether the System Agreement has been violated, there currently exists no FERC order that has found that the Operating Committee's decision is in compliance with the System Agreement. In the absence of such FERC determination, the Commission can scrutinize the prudence of the Operating Committee's decision without

violating the Supremacy Clause insofar as that decision affects retail rates. [App. 65a.]

The LPSC then determined that ELI did not consider the effect of the System's treatment of ERS units on its retail rates in Louisiana after August 5, 1997, and that the company failed to minimize its operating costs by continuing such treatment. App. 73a-74a. Moreover, the LPSC stated that ELI's duty to avoid imprudent costs includes the duty to follow the criteria set in the System Agreement to determine the available status of ERS units after August 5, 1997. It found that the Operating Committee's decision was made without complete or accurate information regarding the costs of returning ERS units to service and without ascertaining "'current and future resource needs, the projected length of time the unit would be in ERS status, [the] projected cost of maintaining such unit, and the projected cost of returning the unit to service'" under the amended System Agreement. *Id.* at 74a. Thus, the LPSC concluded that ELI knew or should have known that the MSS-1 payments made after August 5, 1997 were unreasonable at the time the payments were made and that it was imprudent for ELI to pay them even though the System had determined that they were due. The decision prevented ELI from recovering these costs from retail customers and thus trapped these costs.

ELI's arguments that the LPSC's review of the MSS-1 Service Schedule is preempted were rejected. The LPSC agreed that it lacked authority to review the reasonableness of ELI's 1996 MSS-1 payments, which are the MSS-1 payments that were included in the test year data that were under consideration in the case below. App. 64a. The LPSC further agreed that it lacked authority to order refunds of those payments in light of FERC's express refusal to order such refunds. *Id.* But the LPSC reasoned that FERC had not considered whether the Operating Committee's decision to use the ERS units in its calculations after August 5, 1997 complied with the amended System Agreement. Rather than

challenge the Operating Committee's decision at FERC, as it had done previously, the LPSC concluded that it had "the authority to assess the prudence of ELI's decision to continue to accord MSS-1 treatment to ERS units subsequent to the FERC Order No. 415 dated August 5, 1997." App. 69a-72a (emphasis omitted).

4. The Louisiana Supreme Court's Decision. ELI filed a petition for judicial review of the LPSC order on February 17, 1999. The district court, however, affirmed the order, stating that the ruling was "well within [the LPSC's] constitutional and statutory authority," and was neither arbitrary nor capricious. App. 22a. ELI appealed to the Louisiana Supreme Court.

In an opinion without citation to *MP&L*, the Louisiana Supreme Court affirmed the district court's decision. It recited the LPSC's two reasons for rejecting preemption: (1) that FERC had not expressly ruled that the Entergy Operating Committee's decision to include ERS units after August 5, 1997 complied with the System Agreement; and (2) that under *Pike County*, the LPSC had jurisdiction to review the prudence of the decision to continue to include ERS units in MSS-1 Service Schedule of the System Agreement after August 5, 1997, even though the LPSC concededly lacked jurisdiction to review the allocation of interstate wholesale costs under that same Agreement. App. 14a-15a. The Louisiana Supreme Court essentially adopted this reasoning.

First, relying on *Pike County* and *NOPSI*, the state court held that the LPSC was "not attempting to regulate interstate wholesale rates" and had not "challenged the validity of the FERC's declination to order refunds of amounts paid in violation of the System Agreement prior to the amendment." App. 19a. Instead, the court held, "the LPSC has merely examined the prudence of ELI's failure to make steps to minimize its MSS-1 payments after the effective date of the amendment to Section 10.02 of the System Agreement." *Id.*

Second, the Louisiana Court agreed with the LPSC that "the FERC's determination encompassed treatment of the ERS units *prior to* the effective date of the amendment" and that "FERC never ruled on the issue of whether ELI's decision to continue to include the ERS units is a prudent one [or] whether ELI must continue to make overpayments to the other Entergy operating companies." App. 19a.

For both of these reasons, the Louisiana Supreme Court affirmed the LPSC's decision that its review of the decision to include the ERS units in MSS-1, a FERC rate schedule, was not preempted. App. 20a.

Justices Kimball, Lobrano, and Traylor dissented. Justice Kimball's dissent pointed out that the majority had acknowledged that (i) the System Agreement is a FERC rate schedule, (ii) that FERC amended the System Agreement to state that ERS units may be included in calculations for MSS-1 payments if a specified condition is met, and (iii) that "FERC has exclusive jurisdiction over the issue of whether ELI has violated the System Agreement." App. 21a. She stated that the LPSC found ELI's decision to continue to include ERS units after August 5, 1997 imprudent, "because the LPSC found that ELI did not meet the conditions imposed in the amended System Agreement." *Id.* Thus, Justice Kimball concluded, "the LPSC is simply trying to do indirectly what it may not do directly, namely, determine that ELI violated a FERC tariff." *Id.*

REASONS FOR GRANTING THE PETITION

This case presents a recurring question under the Federal Power Act that has been decided in sharp conflict with this Court's prior decisions and those of all other courts, with the exception of the United States Court of Appeals for the Fifth Circuit. The Louisiana Supreme Court established a broad exception to FERC's exclusive jurisdiction over wholesale rates of electricity under the Federal Power Act. It held that

until FERC holds otherwise, states have jurisdiction to determine whether a FERC rate schedule has been violated, and more specifically, to determine whether a utility that is part of an integrated, multi-state power system is imprudent for failing to "minimize" the costs incurred under a rate schedule approved by FERC. App. 20a.

Under this holding, each state served by a multi-state utility system may do what this Court held to be preempted in *MP&L* and *Nantahala* – effectively re-litigate FERC-approved rates and cost allocations and "trap" FERC-mandated costs – subject only to state court review. Other states in the Entergy system and in other multi-state power systems may be forced to follow suit to protect the interests of their consumers. The result will be a patchwork of parochial rulings that is the antithesis of what Congress intended in enacting the Federal Power Act. This decision is worthy of the Court's review because it conflicts with decisions of this Court, is the subject of a conflict in the lower courts, and is critically important to the administration of the federal statute governing regulation of the electric power industry.

I. THE DECISION BELOW CONFLICTS WITH *MP&L*, *NANTAHALA*, AND OTHER DECISIONS OF THIS COURT, THE LOWER COURTS, AND FERC.

Bulk power arrangements among utilities are "particularly likely to affect more than one State, " and "uncontrolled [state] regulation" of utilities in multi-state systems can "patently interfere with broader national interests." *Arkansas Elec. Co-op. Corp.* v. *Arkansas Pub. Serv. Comm'n*, 461 U.S. 375, 377 (1983). In the Federal Power Act, accordingly, Congress established FERC as a single, neutral forum to assure that wholesale rates and contracts affecting such rates are "just, reasonable, and nondiscriminatory," and to balance the interests of shareholders and ratepayers in setting wholesale rates and allocating the prudent wholesale costs

among utilities serving different states.[4] See 16 U.S.C. §§ 824d, 824e; *FPC* v. *Hope Natural Gas Co.*, 320 U.S. 591, 603 (1944). State regulation – which would impair interstate commerce by allowing the litigation and re-litigation of the reasonableness of wholesale power rates and interstate cost allocations in multiple state forums – is forbidden. *Arkansas Elec. Co-op. Corp.*, 461 U.S. at 377. The Act protects local interests by giving states and municipalities rights to participate in FERC proceedings and to file complaints with FERC. 16 U.S.C. §§ 824d, 824e, 825e.

"It is common ground that if FERC has jurisdiction over a subject, the States cannot have jurisdiction over that subject." *MP&L*, 487 U.S. at 377 (Scalia, J., concurring). This Court has construed the Federal Power Act to give FERC "plenary jurisdiction" to make all determinations required to regulate wholesale rates and to allocate costs among affiliated utilities, regardless of the "impact" on state regulation. See *FPC* v. *Southern Cal. Edison Co.*, 376 U.S. 205, 215-16 (1964). See also *Montana-Dakota Utils. Co.* v. *Northwestern Pub. Serv. Co.*, 341 U.S. 246 (1951). "FERC's exclusive jurisdiction applies not only to rates but also to power allocations that affect wholesale rates. . . . States may not bar regulated utilities from passing through to retail consumers FERC-mandated wholesale rates." *MP&L*, 487 U.S. at 371-72 (citation omitted). The filed-rate doctrine and other preemption principles "enforce the exclusive jurisdiction vested by Congress in FERC." *Nantahala*, 476 U.S. at 966. However the state characterizes its action, it is preempted if its "effect" is to interfere with FERC's interstate "allocation of costs." *Maryland* v. *Louisiana*, 451 U.S. 725, 749-50 (1981).

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[4] *See* 16 U.S.C. § 824 (providing FERC with exclusive jurisdiction to regulate the "transmission" and the "sale of electric energy at wholesale in interstate commerce"); *FPC* v. *Southern Cal. Edison Co.*, 376 U.S. 205, 215-16 (1964) (FERC has plenary jurisdiction to regulate all aspects of wholesale transactions, regardless of the impact on state regulation).

In this case, in violation of these principles, the Louisiana Supreme Court held that the LPSC had jurisdiction to decide that "ELI's failure to make steps to minimize its MSS-1 payments after the effective date of the amendment to Section 10.02 of the System Agreement" was imprudent. App. 19a. The state court rested its holding on two purported exceptions to FERC's exclusive jurisdiction. First, the state court held that the *Pike County* exception, which allows states to determine the prudence of certain decisions by utilities to make purchases at FERC-filed rates, applied. *Id.* at 15a-17a. Second, the Louisiana court held that the LPSC had jurisdiction, because "FERC never ruled on the issue of whether ELI's decision [sic] to continue to include the ERS units is a prudent one." *Id.* at 19a.[5] In *MP&L* and *Nantahala*, however, this Court affirmed the filed-rate doctrine in this very context. It expressly rejected the application of the *Pike County* exception to rate schedules governing the allocation of costs within integrated, multi-state systems, and it held that States are prohibited from regulating in areas governed by FERC even if FERC has not yet acted.

In *MP&L*, the Court reviewed a judgment of the Mississippi Supreme Court that required the state utility commission to examine the prudence of the management decisions that led Middle South Utilities (now Entergy) to construct a nuclear power plant called Grand Gulf 1. The Mississippi court stated that it had become "obvious" by the early 1980's, that "both the cost and demand projections related to Grand Gulf were terribly incorrect," and thus ordered a prudence "review" to determine whether the system "acted reasonably when they constructed Grand Gulf 1, in light of the change in demand for electric power . . . and the sudden escalation of costs." *State ex rel. Pittman* v. *Mississippi Pub. Serv. Comm'n*, 506 So. 2d 978, 986, 987

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[5] The decision was not, of course, ELI's, but that of the System Operating Committee that administers the System Agreement.

(Miss. 1987) (en banc); *MP&L*, 487 U.S. at 368. This review would have decided the extent to which MP&L had been imprudent with respect to Grand Gulf expenditures and thus the extent to which Grand Gulf costs should be "trapped" and borne by the utility's shareholders, rather than "passed on to MP&L's retail customers." *MP&L*, 487 U.S. at 372 n.12. The state court also held that "'[a]s to those matters not resolved by the FERC, state regulation is *not preempted provided that* State regulation would not contradict or undermine FERC determinations and federal interests, or impose inconsistent obligations on the utility companies involved.'" 506 So. 2d at 986.

MP&L, however, held that the state court's judgment was preempted by federal law. It reaffirmed this Court's earlier decision in *Nantahala* and held that the Federal Power Act and the Supremacy Clause "preclude [such a] review of MP&L's managerial prudence." 487 U.S. at 369. It held that a state retail ratemaking body "may not enter an order 'trapping' the costs MP&L [and other system operating companies are] mandated to pay under the FERC order allocating Grand Gulf power or undertake a 'prudence' review for the purpose of deciding whether to enter such an order." *Id.* at 372 & n.12. "States may not alter FERC-ordered allocations of power by substituting their own determinations of what would be just and fair." *Id.* at 371. See also *Nantahala*, 476 U.S. at 970.

In *MP&L*, this Court made it explicit that FERC had exclusive jurisdiction to determine the prudence of decisions of MP&L and other system operating companies. All such "prudence" claims, the Court said, were matters "FERC easily could have considered in determining whether to permit [the system] to recoup 100% of the costs of Grand Gulf in the wholesale rates it charged to the four operating companies and in allocating Grand Gulf Power" among those companies. *MP&L*, 487 U.S. at 375. The Court explicitly rejected the argument that state commissions have authority to bar

recovery of FERC-mandated wholesale costs on grounds that could have been raised before FERC. *Id.* At bottom, "[t]he reasonableness of rates and agreements regulated by FERC may not be collaterally attacked in state or federal courts. The only appropriate forum for such a challenge is before the Commission or a court reviewing the Commission's order." *Id.*

Equally to the point, the *MP&L* Court specifically recited the *Pike County* exception and rejected its application to the case before it. As the Court observed, that exception applies only if a utility unreasonably purchases high-cost power at FERC-approved rates when the utility "had the legal right to refuse to buy that power." *Id.* at 374. Just as here, in *MP&L*, the utilities had no choice but to accept the allocation of costs and power in the FERC-approved rate schedule: "[I]f the integrity of FERC regulation is to be preserved, it obviously cannot be unreasonable for MP&L to procure the particular quantity of high-priced Grand Gulf power that FERC has ordered it to pay for." *Id.* All nine members of the Court recognized that although FERC determines only the seller's prudence in an ordinary bilateral transaction, FERC necessarily determines the prudence of buyer and seller when, as here, the power supply arrangements are those of an integrated power pool. *Id.* at 357, 363, 374-75; *id.* at 378 (Scalia, J., concurring); *id.* at 386 (Brennan, J., dissenting). See also *AEP Generating Co.*, 36 FERC ¶ 61,226 (1986); *AEP Generating Co. & Ky. Power Co.*, 38 FERC ¶ 61,243 (1987).

Similarly, in *Nantahala*, this Court held that state retail rate orders may not disregard FERC's allocation of low-cost power among operating companies in an affiliated, multi-state system in setting retail rates. This allocation was part and parcel of FERC's exclusive authority to determine wholesale rates, because it "determine[d] the amount of low-cost power that [Nantahala] may obtain, and FERC required Nantahala's

wholesale rate to be filed in accordance with that allocation." 476 U.S. at 967. Thus, the Court explained:

> The filed rate doctrine ensures that sellers of wholesale power governed by FERC can recover the costs incurred by their payment of just and reasonable FERC-set rates. When FERC sets a rate between a seller of power and a wholesaler-as-buyer, a State may not exercise its undoubted jurisdiction over retail sales to prevent the wholesaler-as-seller from recovering the costs of paying the FERC-approved rate. *Such a "trapping" of costs is prohibited.* Here, [the wholesaler as seller] cannot fully recover its costs of purchasing at the FERC-approved rate if [the state commission's] order is allowed to stand. [*Id.* at 970 (emphasis supplied).]

In *Nantahala*, too, the Court expressly found the *Pike County* exception inapplicable. "Without deciding this issue," the Court assumed "that a particular quantity of power procured by a utility from a particular source could be deemed unreasonably excessive if lower cost power is available elsewhere, even though the higher cost power actually purchased is obtained at a FERC-approved, and therefore reasonable, price." *Id.* at 972 (emphasis ommitted). Nantahala, however, "could not have treated itself as having access to any more low-cost entitlement power than it is eligible to include under FERC's interpretation of what would be a fair allocation," *id.* at 972-73; accordingly, *Pike County* did not apply.

MP&L and *Nantahala* govern this case. This authority precludes the argument that the LPSC or the state court can decide that ELI imprudently failed to minimize its MSS-1 payments. Under the System Agreement, the Entergy Operating Committee determined whether ERS units should be included in MSS-1 payment calculations. The System Agreement – which is a binding FERC rate schedule – governs ELI's costs. If the LPSC wishes to challenge that determination, it must do so before FERC, which has

exclusive jurisdiction to decide whether its rate schedule, the System Agreement, was violated or imprudent. Indeed, the FERC proceedings addressing the inclusion of ERS units in MSS-1 payment calculations prior to August 5, 1997, demonstrate that FERC has jurisdiction over this question and that the state action here is preempted. As *MP&L* and *Nantahala* hold, the *Pike County* exception has no application in these circumstances.

The Louisiana Supreme Court also erred in concluding that the LPSC had jurisdiction to assess the prudence of the Operating Committee's decision to include ERS units in MSS-1 payment calculations, because "FERC never ruled on the issue of whether ELI's decision [sic] to continue to include the ERS units is a prudent one." App. 19a. In essence, the court is saying that the LPSC can evade FERC's exclusive jurisdiction simply by deciding not to file a complaint with FERC challenging the Operating Committee's determination under Section 10.02 of the System Agreement. In *MP&L*, this Court considered and rejected the Mississippi court's holding that "the pre-emptive effect of FERC jurisdiction turned on whether a particular matter was actually determined in the FERC proceedings." 487 U.S. at 374 (citing 506 So. 2d at 986). The Court explained that it has "long rejected this sort of case-by-case analysis of the impact of state regulation upon the national interest in power regulation cases." *Id.* (internal quotation marks omitted) (quoting *Nantahala*, 476 U.S. at 966). Thus, "[t]he reasonableness of rates and agreements regulated by FERC may not be collaterally attacked in state or federal courts. The only appropriate forum for such a challenge is before the Commission or a court reviewing the Commission's order." *Id.* at 375.

Ultimately, in *MP&L*, the Court concluded that the issue of prudence was not discussed in FERC proceedings or on review of FERC orders "because no party raised the issue, not because it was a matter beyond the scope of FERC's

jurisdiction." *Id.* at 375. Similarly here, the LPSC's failure to challenge the Operating Committee's decision to include ERS units in MSS-1 payments after August 5, 1997 does not deprive FERC of exclusive jurisdiction. The LPSC simply "cannot evaluate . . . the prudence of [the] decision to [include ERS costs in MSS-1 payment calculations] without traversing matters squarely within FERC's jurisdiction." *Id.* at 376.

The decision below conflicts not only with this Court's precedent, but also with the decisions of numerous state supreme courts. In addition to the numerous such decisions that hold that the filed-rate doctrine requires that FERC-regulated expenses be treated as reasonable operating expenses in setting retail rates,[6] at least five state supreme courts that have held that FERC's jurisdiction preempts states from rejecting FERC-mandated costs on prudence grounds. See, *e.g.*, *General Motors Corp.* v. *Illinois Commerce Comm'n*, 574 N.E.2d 650, 655-58 (Ill. 1991) (filed rate doctrine applies to costs associated with procurement of gas and state commission has no authority to conduct prudence review of such costs); *Maine Yankee Atomic Power Co.* v. *Maine Pub. Utils. Comm'n*, 581 A.2d 799, 803-04 (Me. 1990) (FERC has exclusive jurisdiction to determine utility's plant decommissioning expense and state commission could not assess the prudence of that expense); *Eastern Edison Co.* v. *Department of Pub. Utils.*, 446 N.E.2d 684, 688 (Mass. 1983) (FERC has exclusive jurisdiction to determine whether utility system was imprudent in failing to take greater steps to minimize risks in construction of plant); *Northern States Power Co.* v. *Minnesota Pub. Utils. Comm'n*, 344 N.W.2d 374, 381-82 & n.17 (Minn. 1984) (FERC has exclusive jurisdiction to assess the prudence of system's decision to

[6] *See Narragansett Elec. Co.* v. *Burke*, 381 A.2d 1358, 1362 (R.I. 1977); *Hopewell Cogeneration Ltd. P'ship* v. *State Corp. Comm'n*, 453 S.E.2d 277, 282 (Va. 1995); *Hamm* v. *Public Serv. Comm'n*, 425 S.E.2d 28, 30 (S.C. 1992); *Appeal of Northern Utils., Inc.*, 617 A.2d 1184, 1186 (N.H. 1992).

cancel a nuclear plant and obtain coal-fired power instead); *Northern States Power Co.* v. *Hagan*, 314 N.W.2d 32, 38 (N.D. 1981) ("it would undermine the supremacy clause and the preemption doctrine for the [state] to indirectly assert jurisdiction over the wholesale rates by investigating the reasonableness of underlying costs in a proceeding involving retail rates").

The courts of appeals for the Fourth, First, Ninth, Eighth, and District of Columbia Circuits, too, have each upheld FERC's exclusive jurisdiction to make prudence decisions that affect FERC rate schedules governing integrated, multi-state power systems. See *Appalachian Power Co.* v. *Public Serv. Comm'n*, 812 F.2d 898 (4th Cir. 1987) (holding that the essence of the *Pike County* exception is choice and therefore that the prudence inquiry that the state commission sought to undertake was an impermissible duplication of the inquiry into the justness and reasonableness of the allocation agreement that was subject to the exclusive jurisdiction of FERC). See also *Public Serv. Co.* v. *Patch*, 167 F.3d 15, 27 (1st Cir. 1998); *Transmission Agency* v. *Sierra Pac. Power Co.*, 295 F.3d 918, 930 (9th Cir. 2002); *Middle S. Energy, Inc.* v. *Arkansas Pub. Serv. Comm'n*, 772 F.2d 404 (8th Cir. 1985); *South Dakota Pub. Utils. Comm'n* v. *FERC*, 690 F.2d 674 (8th Cir. 1982) (per curiam); *Anaheim, Cal.* v. *FERC*, 669 F.2d 799 (D.C. Cir. 1981).[7]

The only decision that provided any support for the LPSC's action here is the decision of the Fifth Circuit in *NOPSI*. In

[7] The only circumstances in which either FERC or the lower courts have permitted states to bar recovery of costs under FERC rate schedules is where FERC regulation has *not* allocated costs to a particular utility, and where the utility has a *choice* to obtain the power from one of many sources. *Pike County Light & Power Co.* v. *Pennsylvania Pub. Util. Comm'n*, 465 A.2d 735, 738 (Pa. 1983). *See also Kentucky W. Va. Gas Co.* v. *Pennsylvania Pub. Util. Comm'n*, 837 F.2d 600, 608-09 (3d Cir. 1988); *Appeal of Sinclair Mach. Prods., Inc.*, 498 A.2d 696, 703 (N.H. 1985).

that case, the court of appeals recognized that a New Orleans City Council order "prevented NOPSI from recovering, in its retail rate, wholesale costs FERC ordered it to incur as a result of its participation in [Grand Gulf 1]." 911 F.2d at 995. The Fifth Circuit also recognized (as the Louisiana Supreme Court did not) that states could not regulate matters that are within FERC's jurisdiction. *Id.* at 1001. However, the Fifth Circuit held that New Orleans had jurisdiction to determine that NOPSI's failure to minimize its allocation of Grand Gulf 1 power was imprudent. *Id.* at 1002. The court concluded that *MP&L* and *Nantahala* established only that "FERC had jurisdiction to determine whether [NOPSI and other system operating companies] acted prudently in deciding to participate in the Grand Gulf venture" initially, and that these cases had not decided "whether FERC has jurisdiction to determine whether NOPSI acted prudently once the Grand Gulf project was underway." *Id.* at 1001. Thus, the court held that states, and not FERC, have exclusive jurisdiction to determine the "prudence" of a utility's failure to "minimize its losses" by "diversify[ing] its supply portfolio." *Id.* at 1001, 1002.

The decision below and *NOPSI* directly contravene this Court's decisions. The fact that the Louisiana Supreme Court and the Fifth Circuit so misread *MP&L*, *Nantahala*, and decades of preemption law – and held that state law review is the only limitation on state subversion of FERC regulation – makes resolution of this conflict and review of this decision a matter of compelling importance.

II. RESOLUTION OF THIS CONFLICT IS A MATTER OF GREAT NATIONAL IMPORTANCE.

Resolution of the conflict described above is a matter of great national importance. In 1935, Congress enacted the Federal Power Act directing FERC to "promote and encourage" "voluntary interconnection and coordination of facilities for the generation, transmission, and sale of electric energy" in the interest of "assuring an abundant supply of

electric energy throughout the United States with the greatest possible economy." 16 U.S.C. § 824a(a). See also Public Utility Holding Company Act, 15 U.S.C. § 79a(a) (finding that sales and exchanges of power within power pools "are not susceptible of effective control by any State"). In the years that followed, utility companies developed power pools and integrated power networks transcending state boundaries. In recent years, the electric utility industry has become much more highly interconnected and is now a national business.

This trend serves Congress' purpose in enacting the Federal Power Act. As one commenter summarized:

> It is universally accepted that interconnection and coordination of the facilities of separate electric companies is in the public interest. Among the most obvious benefits of such coordination are (1) the exploitation of economies of scale in building generating and transmission facilities; (2) the avoidance of unnecessary duplication of facilities; (3) the ability to place generating facilities at the most advantageous sites, regardless of ownership; (4) increased reliability because of the availability of emergency support from interconnected systems; and (5) operating economies which can be achieved by dispatching the lowest cost generation, regardless of ownership, to serve demands on the interconnected and coordinated systems. [K. Duffy, *Will the Supreme Court Lose Patience With Prudence?* 9 Energy L.J. 83, 98-99 (1988).]

See also Regional Transmission Organization, 65 Fed. Reg. 809 (Jan. 6, 2000) (codified at 18 C.F.R. pt. 35) (FERC Order No. 2000) (addressing the economic and service benefits of consolidation of small independent electricity transmission systems into large Regional Transmission Organizations). As a result, "[t]he necessity for federal leadership in securing planned coordination of the facilities of the industry which alone can produce an abundance of electricity at the lowest

possible costs" is as pressing now as it was in 1935. S. Rep. No. 74-621, at 17 (1935).

This case is like *MP&L* and *Nantahala* in that here, as in those cases, the lower court embraced a sweeping exception to well-settled principles that would subvert the orderly scheme that Congress has created and impede fulfillment of Congress' stated purpose. Under this exception, each FERC cost allocation could be re-litigated in each state served by a multi-state power system, and states could interpose "local" parochial interests to preclude the integrated, multi-state planning that the Federal Power Act seeks to encourage. See Duffy, *supra* at 99 ("[a] pooling arrangement simply will not work if each participant continually seeks to maximize its own benefits or minimize its own costs at the expense of the other participants").

A state can always claim that a utility should have minimized its losses by purchasing lower-cost power or refusing to accept its allocated share of the costs of the multi-state system. "Only FERC, as a central regulatory body, can make the comprehensive public interest determination contemplated by the [Federal Power Act] . . . . Lodging exclusive authority in FERC to consider the merits of the [allocation] thus forecloses the potential for differing state pronouncements regarding an agreement involving utilities regulated by various states." *Appalachian Power Co.*, 812 F.2d at 905. See also *Arkansas Elec. Co-op. Corp.*, 461 U.S. at 377; *Southern Cal. Edison Co.*, 376 U.S. at 215-16; *Public Utils. Comm'n* v. *Attleboro Steam & Elec. Co.*, 273 U.S. 83, 89-90 (1927) (expressing concern about parochial state regulation that burdens interstate commerce by requiring exclusive federal regulation of all wholesale power transactions), *overruled on other grounds by Arkansas Elec. Co-op Corp.* v. *Arkansas Pub. Serv. Comm'n*, 461 U.S. 375 (1983); *Massachusetts, Dep't of Pub. Utils.* v. *United States*, 729 F.2d 886, 888 (1st Cir. 1984) (Breyer, J.) (each state would seek to "benefit[] its residents to the detriment of its

neighbors"). When the interests of several states are at odds because of their participation in a multi-state power system and where a decision of one state in favor of its citizens is likely to have an adverse effect on the citizens of other participating states, FERC's jurisdiction is most necessary. That critically important necessity is ignored and thus threatened by the state court decision in this case.

Indeed, related events in Louisiana underscore the threat to the regime of the Federal Power Act, for the LPSC's assertion of authority over FERC-jurisdictional issues in this case was not a one time event, but part of an emerging pattern that appears to represent an overall strategic plan. In another matter, the same special counsel to the LPSC in the case below and in the ERS proceedings at FERC advised the LPSC that when "the Louisiana Commission has a problem with what FERC wants to do" and when it faces "a matter of rather large consequence to the LPSC," the LPSC should not merely participate in proceedings before FERC, but should act in its own right. LPSC Sept. 19, 2001 Business and Executive Session Tr. at 78. Special counsel advised that "if somebody wanted to try to stop the LPSC, . . . it would happen on Louisiana turf." *Id.* at 83.

The LPSC is thus now using its asserted jurisdiction over ELI's prudence to re-determine matters that are within FERC's jurisdiction. Specifically, the LPSC filed a complaint at FERC that contended that the Entergy system has failed to achieve the "rough" production cost equalization required by FERC and that modifications to the System Agreement are required to make it just, reasonable, and nondiscriminatory within the meaning of the Federal Power Act,[8] and FERC is now conducting a massive proceeding in which it is addressing these issues and related issues raised by other state utility commissions that regulate different Entergy operating

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[8] *Louisiana Pub. Serv. Comm'n & the Council of the City of New Orleans* v. *Entergy Corp.*, 98 FERC ¶ 61,135, at 61,390 (2002).

companies.[9] But rather than await and accept the outcome of this FERC proceeding, the LPSC has instituted a separate proceeding in which it is investigating, inter alia, whether "the production costs of the Entergy operating companies [are] equalized, or roughly equalized" and if not, whether "[ELI] acted imprudently in failing to seek changes in the [system] agreement that would bring about the appropriate cost equalization" and in which it would order rate reductions and refunds to the extent that such "imprudence" is found.[10] This proceeding requires the Entergy System to litigate the same matters before the LPSC that are pending before FERC.

The LPSC's other actions dramatically underscore the great national importance of resolving the issues presented in this Petition. Unless the Louisiana Supreme Court's holding is reviewed and reversed, the range of circumstances in which the LPSC and other state commissions can assert parochial interests to disrupt the interstate allocations of bulk power supply is virtually unlimited. The federal scheme for regulation of the electric power industry is profoundly endangered by the holdings in this case and in *NOPSI*.

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[9] 98 FERC at 61,392-93

[10] *Investigation Of Retail Issues Related Entergy System Agreement Billings*, No. U-25888, slip op. at 1 (La Pub. Serv. Comm'n Jan. 4, 2002).

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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APPENDICES

APPENDIX A

SUPREME COURT OF LOUISIANA

No. 2001-CA-1725

ENTERGY LOUISIANA, INC.

v.

LOUISIANA PUBLIC SERVICE COMMISSION, et al.

Filed April 3, 2002

Rehearing Denied May 24, 2002.

JOHNSON, Justice.*

Entergy Louisiana, Inc. ("ELI") filed suit in the Nineteenth Judicial District Court for the Parish of East Baton Rouge seeking a stay or injunctive relief with respect to portions of Order No. U-20925-G issued by the Louisiana Public Service Commission ("LPSC"). By its Order, the LPSC prohibited ELI from including generating units which are in Extended Reserve Shutdown status in the calculation of reserve equalization payments under Service Schedule MSS-1 of the Entergy System Agreement. The LPSC further ordered ELI to credit the overpayments back to its customers. The district court upheld the Order, finding that the LPSC's findings were neither arbitrary nor capricious and that the entity had acted within its constitutional and statutory authority. ELI appealed

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* Retired Judge Robert L. Lobrano, assigned as Justice *Pro Tempore*, participating in the decision.

that judgment pursuant to La. Const. Art. IV, § 21(E).[1] The sole issue presented for review is whether the LPSC is federally preempted from assessing the prudence of ELI's decision in continuing to include the ERS units in its MSS-1 calculations. After a thorough review of the record, briefs, and relevant authorities, we hold that the LPSC is not precluded from assessing the prudence of ELI's actions and that the LPSC's ruling was not arbitrary or capricious or clearly erroneous. Accordingly, we affirm the LPSC's ruling.

FACTS AND PROCEDURAL HISTORY

Background

The LPSC is an independent regulatory agency created by the Louisiana Constitution. It exercises regulatory authority over most retail electric rates and charges in Louisiana. Pursuant to La. Const. Art. IV, § 21, the LPSC has the power to regulate common carriers and public utilities in the State of Louisiana. LSA-R.S. 45:1163 provides in pertinent part:

> A. The Commission shall exercise all necessary power and authority over any street railway, gas, electric light, heat power, waterworks, or other local public utility for the purpose of fixing and regulating the rates charged or to be charged by and service furnished by such public utilities.

The Federal Energy Regulatory Commission ("FERC") is an independent regulatory agency within the United States Department of Energy which regulates, *inter alia,* the

[1] La. Const. Art. IV, § 21(E) provides in pertinent part:

> Appeal may be taken in the manner provided by law by any aggrieved party or intervenor to the district court of the domicile of the commission. A right of direct appeal from any judgment of the district court shall be allowed to the supreme court. These rights of appeal shall extend to any action by the commission, including but not limited to action taken by the commission or by a public utility. . . .

transmission and sale of electric energy at wholesale in interstate commerce. *See* 16 U.S.C.A. §§ 824 *et seq.;* 42 U.S.C.A. §§ 7101 *et seq.* The Federal Power Act defines "sale of electric energy at wholesale in interstate commerce" as the "sale of electric energy to any person for resale." 16 U.S.C.A. § 824(d). However, the Federal Power Act limits federal regulation of electric utilities engaged in interstate commerce "to those matters which are not subject to regulation by the States." 16 U.S.C.A. § 824(a).

ELI is an electric public utility wholly owned by Entergy Corporation, which also owns four other operating companies: Entergy Arkansas, Inc., Entergy Gulf States, Inc., Entergy Mississippi, Inc., and Entergy New Orleans, Inc. ELI operates in forty-three Louisiana parishes. The five operating companies plan, construct, and operate their collective electric generating and transmission facilities as a single, integrated system serving parts of Louisiana, Arkansas, Mississippi, and Texas. The costs and benefits of the coordinated operation of this interstate system are distributed among the operating companies pursuant to a rate schedule known as the Entergy System Agreement ("System Agreement").[2] The System Agreement governs many of the transactions among the operating companies, and its general purpose is set forth in Article III of the Agreement, which states:

> The purpose of this Agreement is to provide the contractual basis for the continued planning, construction, and operation of the electric generation, transmission and other facilities of the [Operating] Companies in such a manner as to achieve economies

[2] The System Agreement was initially entered into on April 23, 1982. At that time, the operating companies included Arkansas Power & Light Company, Gulf States Utilities Company, Louisiana Power & Light Company, Mississippi Power & Light Company, New Orleans Public Service Inc., and Entergy Services, Inc. The Agreement became effective August 1, 1982.

> consistent with the highest practicable reliability of service, subject to financial considerations, reasonable utilization of natural resources and minimization of the effect on the environment. This Agreement also provides a basis for equalizing among the companies any imbalance of costs associated with the construction, ownership and operation of such facilities as are used for the mutual benefit of all the [Operating] Companies.

The System Agreement is a tariff approved by the FERC, and any revisions or amendments to the Agreement/tariff must be approved by the FERC. The overall administration of the Agreement is carried out by the Entergy Operating Committee, pursuant to Section 2.06 of the System Agreement. The Agreement is a binding contract on all of the operating companies, and pursuant to Section 1.01, termination of participation in the Agreement by any of the companies requires ninety-six months (eight years) written notice to the other companies.

The System Agreement allows the operating companies, among other things, to enter into arrangements among themselves to exchange resources. For instance, if one company is unable to meet the energy requirements for its system, it may make arrangements with one of the other companies to use its facilities and/or energy supply. The arrangements for such exchanges must be in the form of a Service Schedule which becomes a part of the System Agreement subsequent to FERC approval.

Since the effective date of the System Agreement, various FERC-approved Service Schedules have been added, one of which is Schedule MSS-1 ("MSS-1").[3] MSS-1 is set forth in

[3] The "MSS" moniker refers to Middle South Services. In the late 1980s, Middle South Services changed its name to Entergy, and MSS is merely a "holdover" from the old company name. The number "1" indicates that it was the first Service Schedule to be added as an ancillary to the System Agreement.

Section 10 of the System Agreement and provides the mechanism for equalizing system reserves among the operating companies. Pursuant to MSS-1, each of the operating companies is responsible for a share of the total Entergy system capability. Each company's share is equal to the ratio of that company's contribution to the system's yearly average peak load. Some of the companies provide more than their calculated share of the system's capability, while others provide less than their calculated share. The companies providing less than their calculated share make deficiency payments to the companies providing more than their share. For example, if one company has reserves (excess capacity), and the other four companies do not, the other four companies may use the reserves, but must make payments to the company for their use. The revenue received from the other four companies is credited against the company with the reserve's payment to the system. Each of the operating companies makes or receives payments based on whether its capacity exceeds, equals, or is less than the system capability for which it is responsible.

In order to be counted as part of a company's capability for determining MSS-1 payments, a generating unit has to be "available" for use by the system. Prior to August 5, 1997, Section 10.02 of the System Agreement provided in relevant part:

> A unit is considered available to the extent the capability can be demonstrated and (1) is under the control of the System Operator, or (2) is down for maintenance or nuclear refueling.
>
> A unit is considered unavailable if, in the judgment of the Operating Committee, it is of insufficient value in supplying system loads because of (1) obsolescence, (2) physical condition, (3) reliability, (4) operating cost, (5)

> start-up time required, or (6) lack of due diligence in effecting repairs or nuclear refueling in the event of a scheduled or unscheduled outage.

Several years after the System Agreement was executed, the operating companies had excess generating capacity. The companies conceived the Extended Reserve Shutdown (ERS) program, which allows the companies to save money (for the customers, as well as for the companies themselves) by placing the excess generating units in an inactive, *i.e.* extended reserve status. Rather than disposing of units not in use, the companies kept twenty-four units on standby to have the power capacity for the future, in the event there was an increase in power demand. By placing the units in extended reserve status, the companies were able to reduce operating staff and maintenance costs and defer costs of repairing the units.[4] The ERS units were not available to serve customers and, therefore, did not meet the definition of "available" in the System Agreement because they were not "down for maintenance or nuclear refueling" as required by the Agreement. Nonetheless, Entergy included the ERS units for purposes of calculating the Entergy operating companies' capability under MSS-1. This treatment of the inactive units resulted in ELI making higher MSS-1 payments than it would have had if the units had not been included in the computation. These costs were passed on to ELI customers in the form of higher retail electricity rates.

The Proceedings Before the FERC

In 1993, Gulf States Utilities Company ("Gulf States") merged with Entergy Corporation, and Entergy sought to amend the System Agreement to add Gulf States as an operating company subsidiary. In connection with the events surrounding the merger, the FERC reviewed the System

[4] By 1999, all of the ERS units, with the exception of one, had either been returned to active service, or was scheduled for return to service.

Agreement and, thereafter, initiated proceedings to determine whether Entergy had violated the Agreement by including the ERS units in its MSS-1 calculations. The LPSC intervened in the FERC proceeding, alleging that Entergy violated the System Agreement by counting the ERS units as available capacity. To remedy the alleged violation, the LPSC sought retroactive refunds for Entergy's Louisiana customers, plus interest.

Following an evidentiary hearing, a FERC administrative law judge concluded that (1) the language of the System Agreement permits Entergy to include generating units in MSS-1 calculations only to the extent that such units are "available;" (2) Entergy's ERS units are not "available" under Schedule MSS-1; and (3) the inclusion of ERS units in MSS-1 calculations is a violation of the System Agreement. *Entergy Services, Inc. and Gulf States Utility Company*, Initial Decision, 70 FERC ¶ 63,018, 1995 WL 85464 (March 3, 1995).

The FERC affirmed the administrative law judge's determination, stating that Entergy does not have "broad, unfettered discretion to decide which units should be eligible for inclusion in Schedule MSS-1 computation." *Entergy Services, Inc. and Gulf States Utilities Company*, Opinion No. 415, 80 FERC ¶61,197 at p. 61,786, 1997 WL 438886 (August 5, 1997). However, the FERC declined to order a refund of overpayments made as a result of the violation, stating:

> By including ERS units in the Schedule MSS-1 computation, Entergy continued the previously-approved equalization approach that was established for excess capacity on the Entergy System. Moreover, if Entergy had not undertaken to reduce costs for its system by implementing the ERS program, these units would have been eligible for inclusion in Schedule MSS-1. We do not believe that the Operating Companies should lose the

> right to have their costs equalized when they take advantage of the ERS program, which, we note, provides very significant benefits for the Entergy system.
>
> * * *
>
> By exercising our discretion not to order refunds, we are simply acting consistent with the equities in this case. Indeed, the record evidence demonstrates that, although Entergy acted in a manner inconsistent with Schedule MSS-1, the end result was just, reasonable, and not unduly discriminatory.

Id. at p. 61,788, 1997 WL 438886. Instead, the FERC approved a proposed amendment to Section 10.02 of the System Agreement, effective August 5, 1997, which allows the ERS units to be considered "available" under certain instances. The amendment provides, in pertinent part:

> A unit is considered available to the extent the capability can be demonstrated and (1) is under the control of the System Operator, or (2) is down for maintenance or nuclear refueling, *or (3) is in extended reserve shutdown (ERS) with the intent of returning the unit to service at a future date in order to meet Entergy System requirements. The Operating Committee's decision to consider an ERS unit to be available to meet future System requirements shall be evidenced in the minutes of the Operating Committee and shall be based on consideration of current and future resource needs, the projected length of time the unit would be in ERS status, the projected cost of maintaining such unit, and the projected cost of returning the unit to service.*

The FERC rejected the LPSC's contention that the language of the amendment is ambiguous and does not limit Entergy's judgment to make decisions on ERS units. The FERC concluded that the amendment serves to rectify the prior Section 10.02's failure to expressly encompass the ERS

program. The FERC subsequently denied the LPSC's request for rehearing. *Entergy Services, Inc. and Gulf States Utilities Company*, FERC Order No. 415-A, 1998 WL 38137 (February 3, 1998).

The Proceedings Before the LPSC

Each year, ELI files with the LPSC certain financial data for the prior year, calculating its cost of services. The LPSC uses the data to determine ELI's future retail rates. When ELI made its rate filing in 1997 for the 1996 test year, it included all of the generating units in ERS status. The LPSC's Special Counsel objected, contending: (1) the overpayments resulting from the inclusion of units in ERS status in MSS-1 should be removed from the 1996 test year operating expenses because they were made in violation of the FERC tariff; and (2) ELI's continued use of ERS units in the MSS-1 calculation violates the amended Section 10.02 of the System Agreement because there is no evidence that Entergy has any "plan" for returning these units to service. Therefore, Special Counsel contended, such overpayments should not be recovered from Louisiana ratepayers. After considering the record, the LPSC ordered ELI to remove from its calculations "all MSS-1 overpayments incurred on or after August 6, 1997." *L.P.S.C. Order No. U-20925-G* at p. 25. The LPSC further ordered ELI to credit the overpayments "back to ratepayers." *Id.*

The LPSC found, *inter alia*, that Entergy's treatment of the ERS units benefits companies such as Arkansas Power & Light, while resulting in increased MSS-1 payment obligations to companies such as ELI and Mississippi Power & Light. The LPSC concluded that there exists no FERC order or other federal regulation that makes it mandatory for ELI to treat ERS units as available after August 5, 1997. The LPSC also concluded that ELI was put on notice by the FERC order that the MSS-1 treatment of ERS units was in violation of the System Agreement, and it resulted in significantly higher

MSS-1 payments by ELI to its sister companies. The LPSC further found that ELI did not consider the effect of increased MSS-1 payments on its retail rates in Louisiana when it decided to continue the MSS-1 treatment of ERS units after August 5, 1997, and the company failed to minimize its operating costs by continuing such treatment.

The LPSC stated that ELI's duty to incur prudent costs and avoid imprudent costs includes the duty to follow the criteria set forth in the amended Section 10.02 in reaching a decision regarding the availability status of ERS units after August 5, 1997. The LPSC found that when the Operating Committee made that decision, it did not have complete or accurate information before it regarding the costs of returning ERS units back to service, nor did the Operating Committee make necessary efforts to ascertain its "current and future resource needs, the projected length of time the unit would be in ERS status, the projected cost of maintaining such unit, and the projected cost of returning the unit to service," all as required by amended Section 10.02. In particular, the LPSC relied upon testimony given by Kenneth Turner, Secretary of the Operating Committee and Director of Resource Planning for Entergy Services, Inc.[5] According to LPSC's findings of fact, in a September 1997 presentation to the Operating Committee, Turner distributed a single sheet of paper showing the estimated cost of return to service of the ERS units including capital investment and five-year operation and maintenance costs on a net-present-value basis. The LPSC found that neither Turner nor his staff prepared any analyses of what it would cost to return the ERS units to service, and, at the time the Operating Committee decided to classify the units as available, Turner had not seen any analyses or studies concerning what it would cost to return the ERS units to

[5] Entergy Services, Inc. is the service company of Entergy Corporation which performs, among other activities, integrated planning for Entergy's Operating Companies.

service. Turner acknowledged that a later conducted Raytheon study [6] was more detailed and reflected better estimates of the cost of returning the ERS units to service, and that in several instances the cost estimates contained in the Raytheon study were more than twice as high as the estimates Turner provided to the Operating Committee. The LPSC further found that the Raytheon study was not available to the Operating Committee when it made the decision to classify the ERS units as available. Finally, the LPSC found that Turner's testimony that he could not give "a day, a week, a month, or even a year for any of the 24[ERS] units . . . [or] a definite date when any of these units . . . will come out" indicates that there was no plan in place to return the units to service. Nevertheless, he asserted that these units would be needed in the "relative near term," which he defined to mean "any time within the next 10 years." Based on these aspects of Turner's testimony, the LPSC concluded that the MSS-1 payments made subsequent to the August 5, 1997 FERC Order were known to ELI, or should have been known, to be unreasonable and imprudent at the time the expenses were incurred.

The LPSC concluded:

> The increased MSS-1 payments resulting from the treatment of ERS units as available under Schedule MSS-1 in violation of a FERC tariff should be removed from the company's calculation of its cost of service, but such disallowance should be prorated because FERC Order No. 415 imposed an obligation on ELI to make those payments for a part of the rate effective period (i.e., up to August 5, 1997).

L.P.S.C. Order No. U-20925-G at p. 25.

[6] In August, 1997, at Entergy's request, Raytheon Engineers & Constructors, Inc. conducted a study estimating the cost of returning the ERS units to service.

ELI filed a petition for judicial review of the LPSC Order on February 17, 1999.[7] After a hearing, the district court affirmed the Order, stating:

> The Court has carefully reviewed this matter and is of the Opinion that the Public Service Commission was neither arbitrary nor capricious in its finding that Entergy could not pass on the ELI overpayment to Louisiana consumers; nor was such ruling preempted by Federal Law and was not based on impermissible data. On the contrary, it was well within its constitutional and statutory authority. Therefore, the Order of the Public Service Commission is upheld.

The district court also granted a preliminary injunction, enjoining implementation and enforcement of the Order, pending a final judgment by this court.

ELI appealed to this court, arguing that the LPSC's actions were arbitrary and capricious and are barred by federal preemption and the doctrine of *res judicata*.

DISCUSSION

The law applicable to judicial review of orders of the LPSC is well-settled. This court has repeatedly stated:

> Initially, as the orders of the Commission are entitled to great weight, they should not be overturned absent a showing of arbitrariness, capriciousness, or abuse of authority by the Commission. Secondly, courts should be reluctant to substitute their own views for those of the expert body charged with the legislative function of rate-making. Lastly, a decision of the Commission will not be overturned absent a finding that it is clearly erroneous or that it is unsupported by the record.

[7] The LPSC order also adopted a "net proceeds" of debt methodology for determining ELI's capital structure. However, that portion of the order is not before this court as it was not appealed to the district court.

Entergy Gulf States, Inc. v. Louisiana Pub. Serv. Comm'n, 00-0336, p. 4 (La.9/1/00), 766 So.2d 521, 525, (citing *Entergy Gulf States, Inc. v. Louisiana Pub. Serv. Comm'n*, 98-1235, p. 6 (La.4/16/99), 730 So.2d 890, 897; *Entergy Gulf States, Inc. v. Louisiana Pub. Serv. Comm'n*, 98- 0881, p. 4 (La.1/20/99), 726 So.2d 870, 874; *Gulf States Util. Co. v. Louisiana Pub. Serv. Comm'n*, 96-0345, p. 2 (La.7/2/96), 676 So.2d 571, 573; *Central Louisiana Elec. Co. v. Louisiana Pub. Serv. Comm'n*, 508 So.2d 1361, 1364 (La.1987)).

This court has further stated:

> The Commission is an expert within its own specialized field and its interpretation and application of its own General Orders, as distinguished from legislative statutes and judicial decisions deserve great weight, because the Commission is in the best position to apply its own General Orders.

Entergy Gulf States, Inc. v. Louisiana Pub. Serv. Comm'n, 00-0336, at p. 4, 766 So.2d at 526, (citing *Entergy Gulf States, Inc. v. Louisiana Pub. Serv. Comm'n*, 98-1235 at p. 6, 730 So.2d at 897, citing *Dixie Elec. Membership Corp. v. Louisiana Pub. Serv. Comm'n*, 441 So.2d 1208, 1210 (La.1983)). In sum, "courts must affirm the Commission's rulings unless they are arbitrary or capricious, an abuse of authority, unsupported by the record, or clearly erroneous." *Entergy Gulf States, Inc. v. Louisiana Pub. Serv. Comm'n*, 00-0336, at p. 4, 766 So.2d at 526, (quoting *Entergy Gulf States, Inc. v. Louisiana Pub. Serv. Comm'n*, 98-1235 at p. 6, 730 So.2d at 897).

The first issue presented for our review is whether the LPSC exceeded its authority when it reviewed ELI's actions regarding including the ERS units in its calculations for MSS-1 payments. In essence, ELI contends that because the issue of violation of or compliance with the System Agreement, a FERC tariff, is peculiarly within the FERC's purview, the

LPSC is barred from determining whether the terms of the Agreement have been met. Conversely, the LPSC contends that its actions is not preempted by federal law because its Order is not in conflict with any federal law.

Was the LPSC Order Barred by Federal Preemption?

In determining whether a state regulation conflicts with the FERC's authority, courts have looked to the "filed rate doctrine," which was created by the United States Supreme Court in *Montana-Dakota Utilities Co. v. Northwestern Pub. Serv. Co.*, 341 U.S. 246, 71 S.Ct. 692, 95 L.Ed. 912 (1951). The doctrine states that *interstate* power rates filed with or fixed by the FERC must be given binding effect by state utility commissions when determining *intrastate* rates. *Montana-Dakota Utilities Co.*, 341 U.S. at 251-52, 71 S.Ct. at 695, 95 L.Ed. at 919. (Emphasis added). In *Nantahala Power & Light Co. v. Thornburg*, 476 U.S. 953, 966, 106 S.Ct. 2349, 2357, 90 L.Ed.2d 943, 954 (1986), the Supreme Court explained the filed rate doctrine, stating:

> FERC clearly has exclusive jurisdiction over the rates to be charged . . . interstate wholesale customers. (Citations omitted). Once FERC sets such a rate, a State may not conclude in setting retail rates that the FERC-approved wholesale rates are unreasonable. A State must rather give effect to Congress' desire to give FERC plenary authority over interstate wholesale rates, and to ensure that the States do not interfere with this authority.

In this case, the LPSC recognized that the "FERC has exclusive jurisdiction over the issue of whether the System Agreement has been violated." *L.P.S.C. Order No. U-20925-G* at 20. Accordingly, the LPSC found that it lacks authority to review the reasonableness of ELI's 1996 MSS-1 overpayments or to order refunds of the same, contrary to the FERC's express refusal to order refunds. However, the LPSC noted that the FERC order did not consider whether the

Operating Committee's decision to use the ERS units in its calculations after August 5, 1997 is in compliance with the System Agreement. Thus, the LPSC concluded that it has "the authority to assess the prudence of ELI's decision to continue to accord MSS-1 treatment to ERS units subsequent to FERC Order No. 415 dated August 5, 1997." *Id.*

The LPSC based its determination upon an "exception" to the filed rate doctrine set forth in *Pike County Light & Power Co. v. Pennsylvania Public Utility Comm'n*, 77 Pa.Cmwlth. 268, 465 A.2d 735, 738 (1983). In that case, Pike County Light & Power Company ("Pike") was a subsidiary of Orange and Rockland Utilities, Inc., a New York State operating utility. Pike's power supply was provided by the parent company through a FERC-approved Power Supply Agreement. Pursuant to an investigation of a proposed supplement to the Agreement/tariff, an administrative law judge concluded that Pike's reliance on the parent company as a source of power represented an abuse of management discretion in consideration of available, alternative, more economical, supplies of electricity. Accordingly, the administrative law judge submitted a recommendation to the Pennsylvania Public Utility Commission reducing Pike's purchased power expense, which resulted in a revenue increase in an amount less than the amount sought in the proposed tariff supplement. The Public Utility Commission adopted the administrative law judge's findings and conclusions, and Pike appealed, arguing that the Public Utility Commission order was barred by federal preemption.

The Pennsylvania court held that, in setting retail rates, a state commission retains power to consider and reject the "wisdom" of a utility company's contract to purchase interstate power at wholesale, even in situations in which the FERC, in setting the wholesale rate, has already found the terms of the interstate arrangement just and reasonable. The court reasoned that while the FERC has exclusive statutory

jurisdiction to set just and reasonable rates, a determination of the *prudence* of the utility company's decision to purchase power from a particular source is not exclusively within the FERC's jurisdiction. Therefore, the court concluded, the filed rate doctrine does not limit the jurisdictional and regulatory authority of a state commission to review a utility's decision to purchase power at a higher (albeit FERC-approved) price, where there are alternative sources of power at a lower price than the FERC-approved price. The court stated:

> The FERC does not analyze [the subsidiary utility company's] cost of service data or purchased power alternatives in making its determination. The FERC focuses on [the parent utility company] to determine whether it is just and reasonable *for that company to charge* a particular rate, but makes no determination of whether it is just and reasonable *for [the subsidiary] to incur* such a rate as an expense. The [Public Utility Commission], on the other hand, has no jurisdiction to analyze [the parent company's] cost of service data and makes no determination as to the reasonableness for [the parent company] to charge its rates. The [Public Utility Commission] focuses on [the subsidiary] and its cost of service data to determine whether it is reasonable for Pike to incur such costs in light of available alternatives. So while the FERC determines whether it is against public interest for [the parent company] to charge a particular rate in light of its costs, the [Public Utility Commission] determines whether it is against the public interest for [the subsidiary] to pay a particular price in light of its alternatives. The regulatory functions of the FERC and the [Public Utility Commission] thus do not overlap, and there is nothing in the federal legislation which preempts the [Public Utility Commission's] authority to determine the reasonableness of a utility

> company's claimed expenses. In fact, we read the Federal Power Act to expressly preserve that important state authority.

Id. at 738.

Moreover, in *New Orleans Public Service, Inc. v. The Council of the City of New Orleans*, 491 U.S. 350, 109 S.Ct. 2506, 105 L.Ed.2d 298 (1989), the New Orleans Public Service, Inc. ("NOPSI"), along with three other operating companies, was a wholly owned subsidiary of a parent company, Middle South Utilities. Each of the operating companies agreed to finance the construction of a new nuclear power plant. Subsequently, a controversy arose over the percentage of each company's share of the construction costs. After a review, the FERC held the NOPSI liable for 17 percent of the costs. NOPSI then applied to the New Orleans City Council, the local ratemaking authority, for retail rate increases designed to pass on to retail customers NOPSI's share of the cost of the nuclear plant. The City Council entered an Order, disallowing some of the rate increase, asserting that NOPSI had negligently incurred the costs. NOPSI sought injunctions in federal and state court to prevent the City Council's Order from taking effect, arguing that the City Council's Order was preempted by federal law.

The federal district court and court of appeal abstained from entertaining the federal injunction, finding that the existence of a state court suit on the same issue required federal abstention. The United States Supreme Court reversed, holding that federal abstention was not required. Although the Court did not address the issue of whether NOPSI's actions subsequent to the FERC order violated the filed rate doctrine, it remanded the case, stating:

> The Council has not sought directly to regulate interstate wholesale rates; nor has it questioned the validity of the FERC-prescribed allocation of power within the Grand

> Gulf system, or the FERC-prescribed wholesale rates; nor has it reexamined the prudence of NOPSI's agreement to participate in [the construction of the power plant] in the first place. Rather, the Council maintains that it has examined the prudence of NOPSI's failure, after the risks of nuclear power became apparent, to diversify its supply portfolio, and that finding that failure negligent, it has taken the normal ratemaking step of making NOPSI's shareholders rather than the ratepayers bear the consequences. Nothing in this is directly or even indirectly foreclosed by the federal statute, the regulations implementing it, or the case law applying it.

491 U.S. at 367, 109 S.Ct. at 2517-18, 105 L.Ed.2d at 316.

On remand, the federal district court held that the City Council's Order was not "facially" preempted by federal law.[8] The federal Fifth Circuit Court of Appeal affirmed, agreeing that the City Council's Order was not preempted by the FERC's Order. The appellate court reasoned that the City Council did not challenge the validity of the FERC's allocation, but merely imposed the consequences of NOPSI's failure to diversify its supply portfolio on NOPSI, rather than

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[8] The federal district court stayed the federal action because the state court had entered judgment in the City Council's favor. In the state court proceedings, the state district court denied the injunction, finding that the Order did not conflict with federal law. The state appellate court affirmed, stating:

> The Council's order on its face, does not violate any express law. In fact, as an administrative ruling, the order is itself akin to law. Moreover, the order specifically provides that it does not intend to affect wholesale ratemaking, which is preempted by federal law, or to undermine the FERC allocation of [the nuclear power plant] power and costs.
>
> The court of appeal expressly declined to address the issue of whether the City Council's Order was preempted by federal law, making it clear that it was deciding the issue of whether an injunction was appropriate.

on its customers. *New Orleans Public Service, Inc. v. The Council of the City of New Orleans*, 911 F.2d 993 (5th Cir.1990).

In the case *sub judice*, like the New Orleans City Council, the LPSC is not attempting to regulate interstate wholesale rates. Nor has the LPSC challenged the validity of the FERC's declination to order refunds of amounts paid in violation of the System Agreement prior to the amendment. Additionally, the LPSC has not challenged ELI's decision to participate in the Agreement. Rather, the LPSC has merely examined the prudence of ELI's failure to make steps to minimize its MSS-1 payments after the effective date of the amendment to Section 10.02 of the System Agreement. There is nothing in the federal statutes or case law that prohibits the LPSC from assessing the prudence of ELI's actions.

Furthermore, the FERC's determination encompassed treatment of the ERS units *prior to* the effective date of the amendment. The FERC refused to order refunds and approved the amendment to Section 10.02 of the System Agreement. The FERC never ruled on the issue of whether ELI's decision to continue to include the ERS units is a prudent one. Nor did the FERC determine whether ELI must continue to make overpayments to the other Entergy operating companies. Also, the FERC did not make it mandatory for the companies to include the ERS units in its MSS-1 calculations. For these reasons, we hold that the LPSC is not precluded from assessing the prudence of ELI's decision to continue to include the ERS units in its calculations for MSS-1 payments.

Was the LPSC Order Arbitrary or Capricious or Clearly Erroneous?

ELI further contends that the LPSC's actions were arbitrary and capricious. As stated above, a reviewing court may reverse the LPSC's ruling if it finds that the Commission's

ruling was arbitrary or capricious or clearly erroneous. *See Entergy Gulf States, Inc. v. Louisiana Pub. Serv. Comm'n*, 00-0336 (La.9/1/00), 766 So.2d 521; *Entergy Gulf States, Inc. v. Louisiana Pub. Serv. Comm'n*, 98-1235 (La.4/16/99), 730 So.2d 890.

As the LPSC pointed out, ELI had two options: (1) continuing to treat the ERS units as available upon meeting the criteria set forth in the amended Section 10.02; or (2) treating the units as unavailable. ELI elected to continue to include the ERS units and pass on the increased costs to its customers in the form of higher retail rates. The LPSC concluded that ELI acted imprudently and determined that ELI, not Louisiana rate payers, should bear the consequences of its decision.

Additionally, the LPSC found that Entergy's Operating Committee did not "exert due diligence in ascertaining the costs and benefits of bringing the ERS units back to service" when it made the decision regarding the availability of the ERS units. The record supports that conclusion. As the LPSC noted, the information that Turner presented to the Operating Committee contained no analysis of the costs and benefits of returning the units to service. Furthermore, the record indicates that no efforts were made to determine when or if the units would be needed. The record is devoid of any attempt by ELI to minimize its costs. Accordingly, we find that the LPSC's finding that ELI acted imprudently by failing to minimize its costs was not arbitrary or capricious and was supported by the evidence.

CONCLUSION

For the reasons set forth above, we hold that the LPSC is not precluded from assessing the prudence of ELI's decision to continue to include the ERS units in its calculations for

MSS-1 payments. We further hold that the LPSC's determination that ELI acted imprudently is supported by the record and is not arbitrary or capricious.

AFFIRMED.

LOBRANO and TRAYLOR, JJ., dissents.

KIMBALL, J., dissents and assigns reasons.

KIMBALL, J., dissenting.

The majority correctly notes that the System Agreement involved in this case is a FERC tariff. As amended by the FERC, it states in part that ERS units may be included in calculations for MSS-1 payments if certain conditions are met. The majority also points out that the LPSC recognized that the FERC has exclusive jurisdiction over the issue of whether ELI has violated the System Agreement. Even though it would be improper for the LPSC to determine that ELI did not meet the conditions and thereby violated the amended System Agreement when it included the ERS units, the LPSC asserts that its action is proper under its authority to assess the prudence of ELI's decision, citing *Pike County Light & Power v. Pa. Public Util. Comm'n*, 77 Pa.Cmwlth. 268, 465 A.2d 735, 738 (1983). In my view, the reason the LPSC found ELI's decision to be imprudent is because the LPSC found that ELI did not meet the conditions imposed in the amended System Agreement. I think that the LPSC is simply trying to do indirectly what it may not do directly, namely, determine that ELI violated a FERC tariff. For these reasons, I dissent.

APPENIDX B

A TRUE EXTRACT OF CIVIL COURT MINUTES

[Filed Mar 9, 2001]

Case No. 458,129 DIV. "D"

ENTERGY LOUISIANA

vs.

LOUISIANA PUBLIC SERVICE COMMISSION

Nineteenth Judicial District Court District Court,
Parish of East Baton Rouge, State of Louisiana,
Division "D," Honorable Janice Clark, Judge
Presiding, On Date of March 9, 2001.

This matter was previously heard on a petition for judical review filed on behalf of plaintiff, submitted to the Court, and by the Court taken under advisement.

In open court, the following oral reasons were dictated this date in this matter, "The Court has carefully reviewed this matter and is of the opinion that the Public Service Commission was neither arbitrary nor capricious in its finding that Entergy could not pass on the ELI overpayment to Louisiana consumers; nor was such ruling preempted by Federal Law and was not based on impermissible data. On the contrary, it was well within its constitutional and statutory authority. Therefore, the order of the Pubic Service Commission is upheld. Judgment to be signed accordingly." (D. Martin, Mon. 3-9-01)

I hereby certify that on this day a notice of the above judgment was mailed by me with sufficient postage affixed, to: [illegible]

Done and signed on 3-12-01

E. Knight
Deputy Clerk of Court

THIS DONE AND SIGNED AT BATON ROUGE, LOUISIANA THIS 9 DAY OF MARCH 2001.

/s/ E. Knight
DEPUTY FOR
Doug Welborn, Clerk of Court
Parish of East Baton Rouge
State of Louisiana

APPENDIX C

LOUISIANA PUBLIC SERVICE COMMISSION

ORDER NO. U-20925-G

LOUISIANA PUBLIC SERVICE COMMISSION, EX PARTE.

Docket No. U-20925-(Formula Rate Plan-1997) In re: Investigation of Louisiana Power & Light Company's rates, charges, services rendered and operations.

(Decided at Open Session held November 18, 1998)

NATURE OF PROCEEDING

The parameters of this Commission review of the revenue requirements for Louisiana Power and Light Company (subsequently termed Entergy Louisiana, Inc.) were established by Commission Order No. U-20925, dated June 15, 1995. Order No. U-20925 adopted a Formula Rate Plan, pursuant to which the Company was required to make annual filings, and rates would be subject to adjustment based upon the Company's filing and the Commission's review of that filing. Implementation of the Formula Rate Plan was pursuant to the Formula Rate Plan Rider (a copy of which is attached to Order No. U-20925 as Appendix I). Changes in rates which are not subject to disagreement amongst the parties become effective during the July billing cycle. Only matters in controversy proceed to hearing. Most of the ratemaking accounting issues in the Second Formula Rate Plan filing have been resolved by agreement amongst the parties. As a result of ELI's Second Formula Rate Plan filing, ELI's jurisdictional retail rates were reduced July 1, 1997 by $67,000,000. The parties have stipulated to a 10.5% rate of return on equity with retroactive application to July 1, 1997.

In the current proceeding, the parties have raised three issues: (1) whether gross or net proceeds of debt should be used in calculating the company's capital structure for ratemaking purposes; (2) whether payments under the System Agreement for the cost of generating units in Extended Reserve Shutdown should be included or excluded from ELI's revenue requirement; and (3) whether consideration should be given to whether the formula rate plan imposes a revenue cap or a rate cap.

JURISDICTION

The Commission exercises jurisdiction in this proceeding pursuant to Article 4, Section 21 of the Louisiana Constitution, and La. R.S. 45:1163(A)(1).

Louisiana Constitution, Article 4, Section 21 provides in pertinent part:

> The Commission shall regulate all common carriers and public utilities and have such other regulatory authority as provided by law. It shall adopt and enforce reasonable rules, regulations, and procedures necessary for the discharge of its duties, and shall have other powers and perform other duty as provided by law.

La. R.S. 45:1163 provides in pertinent part:

> A. (1) The Commission shall exercise all necessary power and authority over any street railway, gas, electric light, heat, power, waterworks, or other local public utility for the purpose of fixing and regulating the rates charged or to be charged by and service furnished by such public utilities.

Pursuant to the Formula Rate Plan ("FRP") adopted in Order No. U-20925, Entergy Louisiana Inc., ("ELI" or "the Company") made an annual filing on May 30, 1997 for the year 1997. On June 6, 1997, the commission received a letter of opposition from Louisiana Energy Users Group ("LEUG"),

opposing ELI's request for authorization to reflect accelerated recovery of certain cost components in the Company's next filed revenue requirements analysis.

During an open session held on June 10, 1997, the Commission ordered ELI to implement an undisputed rate reduction of $54,585,000 effective beginning with the first billing cycle on or after July 1, 1997, which rate decrease will be implemented and allocated in the same manner as the Commission allocated the previous rate decrease in this docket, i.e. on a base revenue contribution basis, an no portion of the rate decrease shall be applied to the interruptible or curtailable portion of any rate; the Commission also voted to deny ELI's Amended Motion for authorization to reflect accelerated recovery of certain cost components in the company's next filed revenue requirement analysis. The Commission allowed all parties an opportunity to file comments. The Commission instructed Special Counsel and Commission consultants to continue to investigate ELI's 1997 FRP filing.

On June 26, 1997, a revised "Rate Adjustments" schedule to ELI's Rider FRP was filed. On July 8, 1997, the Commission issued Consolidated Order No. U-20925-D, U-22092, regarding the decision made at the June 10, 1997 Business and Executive Committee; a Corrected Consolidated Order was issued on July 25, 1997. Motions for intervention out-of-time were filed by several corporations, including Alliance for Affordable Energy, Union Carbide Corporation and Marathon Oil Company. On October 2, 1997, a Notice of Status Conference and Notice of Proposed Intervention was issued by the presiding Administrative Law Judge. The report of that status conference, sent on October 22, 1997, notified all parties of the following procedural schedule: deadline of November 14, 1997 for filing parties' comments, and for Special Counsel's and Intervenors' testimony; November 24, 1997 deadline for ELI to file its responses to Special Counsel and Intervenor testimony; December 30, 1997 deadline for cross rebuttal testimony of Special Counsel

and Intervenors; January 20, 1998 deadline for Special Counsel's and Intervenors' rebuttal testimony; February 4, 1998 deadline for ELI's reply to Special Counsel and Intervenors' rebuttal; February 12, 1998 for filing Pre-Hearing Briefs, and hearing dates of the week of February 16, 1997. Parties filed documents and briefs pursuant to the above procedural schedule. A hearing was had in the matter on February 16-17, 1998. Parties filed Post-Hearing briefs on April 14, 1998, and at the request of the parties, Reply Briefs on May 20, 1998.

A Proposed Recommendation was issued by the Administrative Law Judge on July 8, 1998. The Exceptions to the Proposed Recommendation filed by Staff and ELI were received on July 23, 1998. On August 7, 1998, ELI and staff filed briefs in opposition to each other's Exceptions to the Proposed Recommendations

POSITIONS OF THE PARTIES

ELI and LSPC's special counsel stated in their Pre-Hearing briefs that a stipulation has been reached on all issues except the following two: (1) whether ELI should use gross or net proceeds of debt in the computation of its capital structure; and (2) whether ELI should be allowed to include costs of generating units in "Extended Reserve Shutdown" status ("ERS") in the calculation of the reserve equalization payments under service schedule MSS-1 of the Entergy System Agreement governing some transactions among the Entergy operating companies—i.e. whether these ERS units are "available" as defined in Section 10.02(a) of the Entergy System Agreement.

ELI argues that it is necessary to use net proceeds of debt in calculating the Company's capital structure in order to allow for the proper amount of recovery of capital costs, stating that the use of gross proceeds leads to insufficient recovery. According to ELI, the Company has only the

amount equal to the net, not gross proceeds to invest in rate base. Special Counsel argues to the contrary, that gross proceeds, not net proceeds of debt, should be used to compute the Company's capital structure. Special Counsel states that use of the gross proceeds methods allows for full recovery, not only of the principal amount of the debt, but also of the issuance costs associated with that debt. ELI's use of net proceeds, according to Special Counsel, artificially increases the equity portion of the capital structure, and hence unnecessarily increases the Company's revenue requirement.

ELI argues that the LPSC is precluded from considering overpayments to other operating companies under MSS-1 of the System Agreement and states that an order granting reduction in operating expenses as requested by Special Counsel would violate the filed rate doctrine, the supremacy clause and principles of *res judicata*, such a claim preclusion. In spite of its finding that Entergy violated the Systems Agreement, FERC declined to order a refund of overpayments under MSS-l. According to ELI, the issue, having therefore been considered and decided by a federal agency, is not amenable to Commission review. Special Counsel contends that since the overpayments resulting from the inclusion of units in Extended Reserve Shutdown in MSS-1 were made in violation of the FERC approved tariff, they should be removed from the ELI's revenue requirement; and that ELI's continued inclusion of ERS units in MSS-1 calculation is in violation of Amended Section 10.02, and hence should not be recovered from Louisiana ratepayers.

LEUG argues that Entergy Louisiana, Inc.'s generating units in extended reserve shutdown should not be included in the calculation of reserve equalization payments under Service Schedule MSS-1 of the Entergy System Agreement. In addition, LEUG raises the issue of whether under Commission Order No. U-10925, the FRP Rider filed by ELI should be amended to reflect that no rate increase under the

FRP Rider and/or relating to Waterford 3 may cause any ELI rate schedule to exceed the rates that were in effect on December 31, 1994.

ALJ RULINGS ON EXCEPTIONS TO THE PROPOSED RECOMMENDATION

The ALJ made the following ruling on the exceptions filed to the Proposed Recommendation: ELI excepts to the ALJ's recommendations on the issues of the use of net proceeds of debt in the company's capital structure and the MSS-1 treatment accorded to ERS units. Concerning the first issue, ELI's exceptions contain no new legal arguments, but merely reiterate that the use of gross proceeds does not allow full recovery of the company's capital costs. This issue has been addressed in the Proposed Recommendation in prior Commission proceedings, and in a FERC proceeding referred to in the Proposed Recommendation. ELI's reurging this argument as an exception does not warrant further discussion.

The Proposed Recommendation concluded that FERC Order No. 415, dated August 5, 1997, made it mandatory for ELI to make increased MSS-1 payments resulting from the MSS-1 treatment of ERS units, but that the FERC-mandated obligation ceased on August 5, 1997. Based on a finding that ELI failed to act prudently and minimize its costs when it *continued* to incur those increased costs after August 5, 1997, when they became optional, the ALJ recommended that the costs incurred *after* August 5, 1997 be disallowed, and that the payments made *before* that due date mandated by FERC should not be altered by this Commission. ELI excepted to this recommendation of a prorated disallowance of ERS payments made by ELI after August 5, 1997, by characterizing the recommendation as displaying parochial interest and misapprehending the law. [Page 2 of ELI's exceptions]. This exception was based on ELI's conclusion that the recommendation would interfere with ELI's FERC-mandated MSS-1 payments.

These conclusions, stated as exceptions, seem incognizant of the basic premise, explicitly stated in the Proposed Recommendation that under the facts and circumstances described in the instant case, this Commission cannot alter a FERC-prescribed obligation. This issue raised in ELI's exceptions, and more specific ones, are discussed in the Proposed Recommendation. ELI is referred to pages 20-37 of the Proposed Recommendation (included in its entirety in this Order under the section on ERS units), addressing: preemption; the delineation of the respective jurisdictional authority of FERC and this Commission; the extent of ELI's obligation under the FERC order; and this Commission's authority to scrutinize ELI's prudence in incurring costs *not* mandated by FERC. A prorated disallowance does not interfere with the FERC-set MSS-1 payments, as explained at length in the Proposed Recommendation.

The Administrative Law Judge adopted the suggestion made by the LPSC Staff in its Exceptions regarding the computing of the time period for the disallowance. As explained above, the ALJ recommended a prorated disallowance of the increased MSS-1 costs incurred after August 5, 1997, and initially recommended that 148/365 of such increased payments be disallowed. This ratio was arrived at based on a calendar test year, where 148 days corresponded to the number of days in a calendar year starting August 6, 1997.[1] Staff points out that pursuant to the provisions of the Formula Rate Plan, adjustments required under the Formula Rate Plan shall be effective as of July 1 of the year in which the filing is made. (Formula Rate Plan

[1] The calculation of test year expenses, and not the effective date of Commission-ordered adjustments, is based on the calendar year under the FRP Rider. The FRP Rider states that the "Evaluation Period", ends on December 31 of the test year.

Rider Schedule FRP §§ 2.B, 2.C).[2] Under Sections 2.B and 2.C of the Rider Schedule FRP, the ERS overpayments is a disputed issue; if the Commission resolves a disputed issue by ordering a Rate Adjustment, then "the final Rate Adjustments shall also reflect the adjustments necessary to recover or credit the estimated revenue [overcollection], that would have resulted had the final Rate Adjustments been implemented initially".[3] Thus, the adjustments made pursuant

[2] Section 2.B of the Rider provides:

> ". . . . the Rate Adjustments filed under the provisions of Section 2.A above, or such corrected Rate Adjustments as may be determined pursuant to the terms of this Section 2.B shall, after verification by the Commission, become effective for bills rendered on and after the first billing cycle of July of the filing year. Those Rate Adjustments shall then remain in effect until changed pursuant to the provisions of this Rider."

Section 2.C, entitled "Resolution of Disputes" provides:

> ". . . . If a dispute is resolved such that there are changes in the Rate Adjustments initially implemented that year pursuant to the above provisions, a revised Attachment A containing such further modified Rate Adjustments shall be submitted to the Commission by LP&L within five days of the Commission's order resolving the dispute. *In addition to reflecting the Commission's ruling on the disputed issues, the final Rate Adjustments shall also reflect the adjustments necessary to recover or credit the estimated revenue increase or decrease, respectively, that would have resulted had the final Rate Adjustments been implemented initially.* Such modified Rate Adjustments shall then become effective for bills rendered on and after the fifth day following the date on which the final rate adjustments are submitted, and shall remain in effect until superseded by Rate Adjustments established in the subsequent Evaluation Report filing."

[3] Section 2.C provides, however, that "[d]isputed issues shall be decided by the Commission, which shall render a ruling on such disputed issues *on or before August 31 of the filing year*". Therefore, this provision contemplates that the Commission will issue a ruling on the ERS overpayment issue on or before August 31, 1997. But pursuant to the procedural schedule in this proceeding agreed to by all parties, including

to an order in this proceedings would become effective July 1, 1997.

Based on this information on the effective date of July 1, 1997, for the adjustments under the 1997 Formula Rate Plan order, the 148/365 ratio suggested in the Proposed Recommendation as a method for prorating the disallowance of increased MSS-1 costs should be modified. All costs incurred by ELI *on or after August 6, 1997*, as a result of the continued MSS-1 treatment of ERS units are disallowed, and will be removed from the company's calculation of its cost of service, to be credited back to the ratepayers. As the rate-effective period commences July 1, 1997, the disallowance should be 329/365. Under Sections 2.B and 2.C of the Rider, all Commission-ordered adjustments in this proceeding are made effective for the period of July 1, 1997 through June, [sic] 30, 1998. [See Sections 2.B and 2.C on p.2 and "Effective Date and Term" at p. 5 of the FRP Rider.]

ELI, in Its Memorandum in Opposition to Staff's Exceptions to the Proposed Recommendation, argues that Staff's position in favor of a post-test year adjustment on the ERS units issue in this proceeding contradicts Staff's position in other proceedings against post-test year adjustments. ELI introduces this argument based on portions of sworn testimony in the Stranded Cost proceeding by Mr. Kahal, Staff expert witness, where he recommends that earnings be "calculated on a historical basis, with no 'negative attrition' adjustment" [ELI's "Memorandum in opposition to Staff's Exceptions, at p.2, citing Surrebuttal Testimony of Matthew I. Kahal of behalf of LPSC, June 1998, LPSC Docket No. U-20925(SC) at 13.] ELI further argues, in a footnote, that reference to sworn testimony in another case is permissible in

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ELI, the hearings in this matter did not commence until February, 1998. Thus, the Commission could not possibly have rendered a ruling on the disputed issue of ERS overpayments on or before August 31, 1997.

briefs and exceptions filed with the Commission, because the exceptions filed by Staff in Docket No. U-22092, Third Earnings Review, contain such references.

First, Mr. Kahal's testimony cited by ELI is not part of the evidence on record in this proceeding. Second, the fact that Staff may have cited sworn testimony of a witness in one proceeding in its exceptions filed in a different proceeding does not constitute a ruling by this Commission that such attempts to introduce evidence outside of the record in the current proceeding are "permissible".[4] The Commission made no such finding or ruling, having never addressed such an issue. Third, this Commission has the authority and the duty to decide whether post-test year adjustments are appropriate on a particular issue in a particular proceeding *based on the evidence on that issue in that proceeding*. The position of the Commission Staff on a different post-test year adjustment matter, expressed in another proceeding, are not binding on the Commission. The analysis below on ERS units addresses the issue of when post-test year adjustments are appropriate and why the evidence warrants an adjustment on the ERS issue in this proceeding.

Staff's Brief in opposition of ELI's Exceptions reiterates its exception concerning the issue of how the disallowance of ERS overpayments should be prorated and supports the Administrative Law Judge's conclusions on the issue of preemption.

This Commission finds that ELI's exceptions and Brief in opposition of Staff's exceptions do not warrant any

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[4] ELI had the opportunity to address this matter by mean of Exceptions and Briefs in Opposition to Staff's Exceptions in Docket No. U-22092, the docket where, according to ELI, Staff attempted to introduce sworn testimony from another proceeding. To raise that matter in this docket adds another layer of arguments based on evidence not on record in this proceeding.

modification to the ALJ's conclusion that the ERS overpayments made by ELI *on or after August 6, 1997* should be removed from the Company's cost of service and credited back to the ratepayers.

COMMISSION RULINGS

The Commission generally adopts the Final Recommendation of the Administrative Law Judge, with one exception. The Commission finds that the "net proceeds" of debt, rather than the gross proceeds, should be used in calculating the capital structure of ELI. Prior determinations the Commission in Entergy Gulf States cases are not binding in this case because, as stated by counsel for ELI in oral argument before the Commission, ELI uses a different method of computing its debt cost than is used by Entergy Gulf States. The Commission believes that the net proceeds method under the particular circumstances of this case will promote fairness.

1. GROSS V. NET PROCEEDS OF DEBT:

Contentions of the Parties

ELI's 1997 FRP filing uses the net proceeds of debt in computing the Company's capital structure. In other words, ELI deducts the costs it incurs in issuing debt, such as bond issuance costs, discounts and call premiums, from the gross proceeds it receives when it issues debt, and uses the "net proceeds", adjusted in the manner described herein, in calculating its capital structure. (In this proceeding call premiums account for almost all of the issuance costs [Tr. 2/16, Kahal at 14]). Special Counsel stated that, both in the 1996 FRP and in this proceeding, Staff did not contest the prudence of these issuance expenses, and in fact acknowledged that these costs should be recovered from the ratepayers. Where Special Counsel and ELI disagreed,

however, was the manner in which these figures should be used in reflecting the Company's capital structure.

The Company's Pre-Hearing and Post-Hearing Briefs stated that the use of gross proceeds leads to insufficient recovery, since the use of gross proceeds increases the debt portion and decreases the equity portion of the capital structure. According to the Company, where the net proceeds of debt are less than the gross proceeds, use of the gross proceeds method will always operate to deprive the utility of an opportunity to recover fully its actual capital costs, because the Company has only the amount equal to the net proceeds, and not the gross proceeds, to invest in rate base. The Company contended that the use of net proceeds is necessary to allow for full recovery of the debt issuance expenses. Special Counsel proposed that the actual amount of the debt (the "gross proceeds" of the debt) that appear in the Company's books should be used for purposes of computing capital structure, stating that this methodology allows a full recovery of all debt issuance and call premium expenses, via amortization, over the life of the new debt issuances. In Special Counsel's view, the full amount of the call premiums will be recovered from the ratepayers under this method; and until issuance costs are fully recovered by the Company, the Company should have an opportunity to earn a debt return on the unamortized balance of the costs. To assure this return, Special Counsel proposed to reduce the Company's debt balance by the amount of the unamortized call premiums for purposes of computing the embedded cost of debt, which, according to Special Counsel, his the result of raising the cost of debt with a concomitant increase in the Company's revenue requirement. The combination of these two procedures, Special Counsel argued, will ensure full recovery of all costs associated with debt issuances and also provide a return on the un-amortized balance of those costs.

Special Counsel contended that ELI's proposal of using net proceeds would have the effect of reducing the debt balance in the capital structure, which would artificially increase the equity portion of the capital structure. Since the rate of return on equity is higher than for debt, the Company's proposal, Special Counsel concluded, results in an increase in revenue requirement.

Special Counsel recommended that the Company's proposal should be rejected for the following reasons: First, Special Counsel's proposal of using gross proceeds would permit full recovery of all debt issuance costs, and no further recovery should be permitted or necessary. Second, in Order No. U-19904, the Commission rejected the use of "net proceeds" by ELI's sister company Entergy Gulf States Inc., and affirmed the ALJ's recommendation which stated:

> Gross proceeds are the amount of debt that actually appear on GSU's books as the principal amount outstanding of Gulf States' debt. Issuance costs are already recovered from the ratepayer is part of the cost of debt. [Direct, Baron, Ex. 1 at 24] Prior to the merger, GSU consistently employed, and the Commission recognized gross proceeds of debt. Use of net proceeds would substitute, in an amount equal to the issuance cost, equity for debt in GSU's capital structure, and thereby increase the Company's return on investment. What took place was not, as use of net proceeds would suggest, the issuance of stock, but rather it was financed as part of the debt issuance. Since the cost of equity is higher then the cost of debt, treatment of the issuance cost in effect as equity would be to the shareholder's benefit and would increase the cost to ratepayers.
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> [Order No. U-21485 dated October 4, 1996 at 16.]

Mr. Kabal, LPSC consultant, was questioned regarding the basis of his recommendation to use the gross proceeds of debt

in computing capital structure, and he replied that while he had not done a formal survey, his understanding was based on fifteen years of testifying on rate of return issues in federal jurisdictions, in several dozen state jurisdictions and in excess of one hundred cases. In each of the cases that Mr. Kahal participated in, the use of the face amount of the debt was the normal basis for capital structure in ratemaking. He stated that he saw no indication in any of the finance texts that he had occasion to consult that net proceeds instead of gross proceeds should be used in capital structure. [Tr. 2/16, Kahal at 16]

Staff also cited a recommendation by a FERC ALJ in Docket No. ER95-1042-000, which reached a similar conclusion and rejected the use of gross proceeds in capital structure by a sister company of GSU.

Special Counsel finally argued that this matter has been litigated twice before this Commission in Orders U-21485 and U-19904 (rate reviews of Entergy Gulf States, ELI's sister company), settled by the Commission, and affirmed on appeal; therefore, the issue should be put to rest and the Commission should reject the use of net proceeds, consistent with its prior orders.

Findings of Fact

1. A utility's cost of capital is the weighted average of the utility's cost of common equity, debt, and preferred stock.

2. The weighted average cost of capital is then applied to the Company's rate base to determine the dollar amount of the return that the Company will be permitted to earn to cover its cost of capital.

3. A utility's capital structure for ratemaking purposes should generally reflect the relative portion of each type of capital.

4. It is assumed, for ratemaking purposes, that generally the various types of capital are invested in rate base in the same proportions as they are available to invest in rate base. [Tr. 2/16, Kahal at 20]

5. The cost of equity is higher than the cost of debt.

6. "The optimal capital structure or the debt capacity for a firm just balances investors' and consumers' interests. While the investor is made less secure as the debt level rises, the consumers' gain more than offsets this disadvantage up to the debt capacity of the utility." Howe, Keith M. And Eugene F. Rasmussen, *Public Utility Economics and Finance*. Prentice-Hall, New Jersey, 1982, p. 103.

7. ELI's 97 FRP filing was made using the net proceeds of debt methodology.

8. The net proceeds of debt methodology utilizes the principal amount of debt net of the cost of issuing the debt or other financial costs.

9. Staff argues that the gross proceeds of debt, rather than the net proceeds of debt, is the proper amount to include in the Company's cost of capital.

10. The gross proceeds of debt represents the face amount of the debt, that is, the principal which the lender is expecting to be repaid.

11. ELI incurs certain costs associated with the issuance of debt, such as issuance costs, discounts, or call premiums.

12. No party to this proceeding has challenged the recovery of these costs from the ratepayer by inclusion in the Company's Revenue Requirement.

13. The gross proceeds methodology provides for the recovery of these expenses in two ways: (1) an annual amortization is added to interest expense; (2) In addition,

for embedded cost of debt calculation purposes, the debt balance is reduced by the unamortized balance, further raising the debt return.

14. The Company recovers all of the call premiums and other debt related expenses plus a debt return on the unamortized balance, until recovered. [LPSC Staff Ex. # 2 at 6]

15. The gross proceeds method fully compensates the Company for all the issuance costs it incurs.

16. Use of the gross proceed method has been adopted by the Commission for another Entergy company, Entergy Gulf States, Inc. In Order No. U-21485, *In Re Annual Monitoring of Gulf States Utility Company's Louisiana Jurisdictional Revenue Requirement Study Under Terms of the Joint Regulatory Proposal Set Forth in Appendix I to Commission Order No. U-19904* (October 4,1996)

17. The Commission's decision to use the gross proceeds methodology was affirmed by the Nineteenth Judicial District Court in *Entergy Gulf States, Inc. v. Louisiana Public Service Commission*, No. Ex: Commission, No. 432,745 (19th JDC, 1998).[5]

18. In a recent proceeding before the Federal Energy Regulatory Commission, the FERC Administrative Law Judge adopted the gross proceeds methodology. *System Entergy Resources, Inc.* Docket No. ER 95-1042-000 76 FERC ¶63,001 (1996)

Legal Analysis

For the purpose of this proceeding involving Entergy Louisiana, Inc., the Commission will adopt the net proceeds method of treating debt cost in determining the capital

[5] Entergy has filed an appeal to the Louisiana Supreme Court of the 19th JDC's ruling.

structure. As counsel for Entergy Louisiana explained in the oral argument before the Commission, ELI does not use the "yield to maturity" method of determining debt cost, as is used by Entergy Gulf States, Inc. Also, counsel for ELI represented that the net proceeds method historically has been used to determine ELI's capital structure. Thus, this case is distinguishable from the Commission's rulings in Entergy Gulf States cases. The Commission finds that the net proceeds method is a fair basis to determine the capital structure for ELI.

2. GENERATING UNITS IN EXTENDED RESERVE SHUTDOWN (ERS) STATUS:

Background

The dispute between the parties on this issue involves the Entergy System Agreement, a FERC-approved tariff that governs certain transactions between the Entergy operating companies. Pursuant to the terms of this tariff, each operating company shares in the costs of the total Entergy system generating capacity based on its own peak demand requirements relative to those of other operating companies. Schedule MSS-1 of the Agreement, set forth in section 10 of the System Agreement, provides the mechanism by which each operating company makes or receives payments based on whether the capacity it owns exceeds, equals or is less than the system capability for which it is responsible. Schedule MSS-1 purportedly equalizes the system reserves bourne by each operating company.

Prior to August 5, 1997, in order to be counted as a part of a company's capability for determining MSS-1 payments, a generating unit had to be "available" for use by the system, as defined in Section 10.01(a) of the Agreement:

> A unit is considered available to the extent the capability can be demonstrated and (1) is under the control of the System Operator, or (2) is down for maintenance or nuclear refueling. A unit is considered unavailable if, in the judgment of the Operating Committee, it is of insufficient value in supplying system loads because of (1) obsolescence, (2) physical condition, (3) reliability, (4) operating cost, (5) start-up time required, or (6) lack of due-diligence in effecting repairs or nuclear refueling in the event of a scheduled or unscheduled outage.

On January 1, 1987, several years after the execution of the System Agreement, the Extended Reserve Shutdown ("ERS") Program was conceived, which allowed the operating companies to place generating units in an inactive status in order to reduce costs by reducing operating staff, maintenance costs, and deferring the costs of repairing units. Since the inception of the ERS program, Entergy included the units in ERS status, including units that do not meet the above definition of available, as if they were "available" within the meaning of Section 10.02 of the System Agreement, for purposes of calculating the Entergy Operating Companies' capability under MSS-1.[6]

In a proceeding involving the inclusion of ERS units in MSS-1 calculations before the Federal Energy Regulatory Commission (*Entergy Services, Inc. and Gulf States Utilities Company*, 70 FERC ¶ 63,018 (1995)), the following issues were addressed by the presiding ALJ: (1) Did Entergy, in fact, violate the System Agreement?; (2) Assuming a violation of the System Agreement, what remedy, if any, is appropriate?; (3) Assuming a violation of the System Agreement, what is the dollar amount of such violation for the entire period that the violation occurred?; (4) Should Service Schedule MSS-1 of the System Agreement be

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[6] *Entergy Services Inc. and Gulf States Utilities Company*, (Opinion No. 415), 80 FERC ¶ 61,197 (8/5/97), Slip Op. at 3-5

amended prospectively to address expressly the ERS issue, and if so, how?[7]

The FERC Administrative Law Judge's conclusion in that proceeding that "the language of the System Agreement permits Entergy to include generating units in Schedule MSS-1 calculations only to the extent that such units are available, that the ERS units were not available under Schedule MSS-1, and that the inclusion of ERS units in the Schedule MSS-1 calculation was a violation of the System Agreement" was affirmed by the full FERC on appeal, in *Entergy Services, Inc. and Gulf States Utilities Company*, (Opinion No. 415), 80 FERC ¶ 61,197 (August 5, 1997).[8] In affirming the ALJ's determination, the FERC stated that "the System Agreement does not afford the Entergy Operating Committee broad, unfettered discretion to decide which units should be eligible for inclusion in Schedule MSS-1 computations".[9]

In considering the ALJ's recommendation, the FERC made the following findings: (1) Entergy violated the System Agreement by treating units in ERS status as available within the meaning of Section 10.02; (2) however, *as among the Entergy operating companies*, no refunds of overpayments made as a result of such violation was necessary; (3) since no refunds were deemed necessary, it was unnecessary to quantify the amounts to be refunded; (4) a prospective amendment to Section 10.02, as proposed by various parties in an Offer of Settlement, would adequately remedy the violation.

That FERC Order (Order No. 415 dated August 5, 1997), also approved a prospective amendment of Section 10.02 of

[7] *Id.*, at 5

[8] *Id.*, at 12

[9] *Id.*

the System Agreement, "effective as of the beginning of the first complete billing cycle following the date of issuance of this order".[10] Section 10.02, as amended, providers, in pertinent part:

> A unit is considered available to the extent the capability can be demonstrated and (1) is under the control of the System Operator, or (2) is down for maintenance or nuclear refueling, or (3) is in extended reserve shutdown (ERS) with the intent of returning the unit to service at a future date in order to meet Entergy System requirements. The Operating Committee's decision to consider an ERS unit to be available to meet future System requirements shall be evidenced in the minutes of the Operating Committee and shall be based on consideration of current and future resource needs, the projected length of time the unit would be in ERS status, the projected cost of maintaining such unit, and the projected cost of returning the unit to service.

Contentions of the parties

ELI's 1997 rate filings, which are the subject of this proceeding, include the payments made by ELI to the other operating companies under MSS-1 of the System Agreement as part of the operating expenses for the test year of 1996. Special Counsel for the Commission contended that: (1) since the overpayments resulting from the inclusion of units in ERS status in MSS-1 were made in violation of the FERC tariff, they should be removed from the 1996 test year operating

[10] The FERC Order provides that, "Schedule MSS-1 is hereby amended, *effective as of the beginning of the first complete billing cycle following the date of issuance of this order*, to clarify the treatment of ERS units as provided in the Offer of Settlement." [Emphasis provided]. The parties have not introduced any evidence concerning when the first billing cycle following the issuance of FERC Order No. 415 began, nor has ELI suggested any effective date other than August 5, 1997, the date of that FERC Order.

expenses; (2) ELI's continued inclusion of ERS units in the MSS-1 calculation violates the amended Section 10.02, and such overpayments should not therefore be recovered from Louisiana ratepayers.

In anticipation of ELI's argument that Special Counsel's request would be barred by the filed rate doctrine, Special Counsel stated that the filed rate doctrine does not preclude the exclusion of these amounts from ELI's 1996 operating expenses because, under *Nantahala Power & Light Co. v. Thornburg*, 476 U.S. 953, 106 S. Ct. 2349 (1986), "[t]he filed rate doctrine ensures that sellers of wholesale power governed by FERC can recover the costs incurred by their payment of *just and reasonable FERC-set rates*". 106 S.Ct. at 2358.[11] Special Counsel reasoned that these overpayments were *not* "just and reasonable FERC-set rates", since they were made in violation of a FERC tariff, as confirmed by the FERC's finding that Entergy violated the System Agreement, by including ERS units in MSS-1 calculations. In Special Counsel's view, the FERC's decision not to order refunds *as among the Entergy operating companies* does not preclude a disallowance of charges paid in violation of a FERC tariff in a retail rate-making proceeding before this Commission.

In response to Special Counsel's first argument, ELI stated that an order by this Commission granting the reduction in operating expanses requested by Special Counsel would violate: (1) the filed rate doctrine; (2) the supremacy clause; and (3) principles of *res judicata*, such a claim preclusion. ELI contended that despite the finding that Entergy violated the System Agreement, the FERC refused to order a refund of those overpayments based on its finding that the violation did not result in unjust, unreasonable or unduly discriminatory rates. Therefore, ELI concluded, the filed rate doctrine would

[11] LPSC Post-Hearing Brief at 13-14, Emphasis provided by Special Counsel.

preclude any modification by this Commission of the payments to be made pursuant to that FERC Order.

ELI further argued that this Commission is without jurisdiction over issues of alleged violation of the System Agreement, as such allegations may only be properly brought before the FERC. ELI averred that Special Counsel's request to remove such overpayments from ELI's revenue requirements is a collateral attack on the FERC Order. Finally, according to ELI, principles of *res judicata*, such as claim preclusion, bar the resolution requested by Staff as the LPSC has once brought before the FERC, what according to ELI is the same issue arising from the same facts, and sought the same relief. Therefore, ELI argued, Staff may not seek resolution of an issue that has already been adjudicated by the FERC.

Special Counsel's second argument that those amounts should be removed from ELI's filings was based on an assertion that ELI has not complied with the new amended provisions of Section 10.02 of the System Agreement. Special Counsel stated that the evidence does not show that ELI or Entergy has any "plan" for returning these units to service as required by the amended provisions of Section 10.02, and hence the inclusion of units in ERS status does not comply with the amended System Agreement. Special Counsel stated that it sought data from ELI to demonstrate that these units would be returned to service and that it was more economic to return these units to service than to build new units or purchase power and energy outside the system, and that no such data was provided by ELI. [LPSC Staff Reply Brief at 10] Staff therefore argued that based on the evidence, the Commission should find that the inclusion of the units in ERS status in MSS-1 calculations is a continued violation of the System Agreement, and the resulting overpayments should consequently be removed from ELI's revenue requirement.

In support of its argument that ELI did not comply with the amended Section 10.02, Special Counsel directed this Commission to Mr. Turner's testimony on the Operating Committee's consideration of the issue of whether to continue to include all the 23 units in ERS status in MSS-1 payments. Special Counsel relied on the following facts testified to by Mr. Turner, the Secretary of the Operating Committee, to argue that the Operating Committee did not consider "current and future resource needs, the projected length of time the unit would be in ERS status, the projected cost of maintaining such unit, and the projected cost of returning the unit to service", as required by the amended Section 10.02: (1) At a meeting held in September 1997, Mr. Turner made a presentation to the Operating Committee, with information contained in a single sheet of paper showing the estimated cost of return to service of the ERS units including capital investment and five year operation and maintenance costs on a net present value basis;[12] (2) neither Mr. Turner nor his staff prepared any analyses of what it would cost to return the ERS units to service;[13] (3) Mr. Turner is not an engineer and would not have been qualified to perform any of the analyses concerning the cost to return these units to service [14]; (4) at the time of the meeting when the Operating Committee made its decision based on Mr. Turner's presentation, Mr. Turner had not seen any analyses or studies concerning what it would cost to retain the ERS units to service; [15] (4) Mr. Turner acknowledged that a study later conducted by Raytheon Engineers and Constructors, Inc. ("the Raytheon Study") was more detailed and reflected better estimates of the cost of

[12] Staff Reply Brief at 11, referring to ELI Ex # 14, KMT Ex. #1, p.8 of 10

[13] *Id.*, referring to Tr. 2/16/98 at 101-103

[14] Staff's Post-Hearing Brief at 17, citing Tr. 2/16/98 at 103

[15] Staffs Post-Hearing Brief at 17, Reply Brief at 12, citing Tr. 2/16/98 at 101

returning the ERS units to service; (5) in several instances the cost estimates contained in the Raytheon Study were more than twice as much as the estimates provided by Turner to the Operating Committee; [16] (6) The Raytheon study was not presented to the Operating Committee at its September 1997 meeting when it made the decision to classify these units as "available"; [17] (7) Mr. Turner could not give "a day, a week, a month, or even a year for any of these 24 [ERS] units . . . [or] a definite date when any of these units on this page [ERS units] will come out . . .";[18] (8) notwithstanding these admissions, Mr. Turner asserted that these units would be needed in the "relative near term", which he defined to mean "any time within the next 10 years." [19]

Based on these aspects of Mr. Turner's testimony, Staff concluded that: (1) the Operating Committee's decision to continue to include ERS units in MSS-1 calculations was based on unreliable information; (2) had the Committee had the more reliable estimates in the Raytheon Study that were more than twice as high as Mr. Turner's estimates in several cases, the Committee may not have found that the ERS units were economic to bring back into service. Therefore, Special Counsel argued, the Operating Committee's decision did not comply with requirements in the new Section 10.02, to consider "current and future resource needs, the projected length of time the unit would be in ERS status, the projected cost of maintaining such unit, and the projected cost of returning the unit to service".

Special Counsel also directed this Commission to the FERC's express statement in Order No. 415, in response to

[16] Staff Reply Brief at 12, citing Tr. 2/16/98 Confidential at 3-4, and LPSC Staff Exhibit Nos. 6 and 7

[17] Staff Reply Brief at 12 citing Tr. 2/16/98 at 106

[18] Staff Reply Brief at 10, citing Tr. 2/16/98 at 100

[19] Staff Reply Brief at 10, citing Tr. 2/16/98 at 101

LPSC's concerns that the amendment to the System Agreement did not "provide the Operating Committee with unfettered discretion". Special Counsel contended that ELI has exercised exactly the kind of unfettered discretion that the FERC Order assured this Commission the Operating Committee did not have, since ELI has not demonstrated through any evidence its "intent to return the units to service at a future date". Special Counsel noted that, in response to Special Counsel's request for data on ELI's plans to return the ERS units to service, ELI could not provide any specific dates or even a year when those units are anticipated to be returned to service; and that, while Mr. Turner acknowledged the same fact,[20] he nevertheless stated that the ERS units would be needed in the "relative near term", which he defined to mean "anytime within the next 10 years". Special Counsel argued that ELI's statement that these units would be needed anytime within the next 10 years, in light of its inability to provide anymore specific evidence is precisely the "unfettered discretion to decide which units should be eligible for inclusion in Schedule MSS-1 computations" that the FERC found the operating committee did not posses.

ELI challenged Special Counsel's second argument that the Company had failed to comply with the amended Section 10.02 on three distinct grounds: (1) according to ELI, Special Counsel has not shown that the Operating Committee's decision was not a good faith decision by ELI to continue to include the ERS units, which decision satisfied the criteria established by the FERC; [21] (2) Special Counsel's allegation that ELI has failed to comply with the amended System Agreement may only be properly brought before the FERC, insofar as the issue involves an interpretation of MSS-1, a FERC rate schedule; [22] (3) and finally, ELI argued that any

[20] Tr. 2/16/98 at 100

[21] ELI Post-Hearing Reply Brief at 24

[22] *Id.*

alleged violation of the August 5, 1997 amendment to the System Agreement cannot serve to reduce operating expenses for the test year of 1996, since post-test-year events may not be reflected in calculating test-year expenses.[23]

Other than its argument that the filed rate doctrine would not deprive this Commission jurisdiction because the MSS-1 payments was not "just and FERC-set rates" but actually violative of the FERC tariff[24], Special Counsel has not briefed the jurisdiction issue. However, Special Counsel continued to urge the removal of the MSS-1 payments from the 1996 test year expenses, and continued to allege a violation of the August 5, 1997 amendment to the System Agreement.

Findings of Fact

19. The Entergy System Agreement is a FERC-approved tariff that governs some transactions between the Entergy operating companies. Pursuant to the terms of this tariff, each operating company shares in the costs of the total Entergy system generating capacity based on its own peak demand requirements relative to those of other operating companies.

20. Schedule MSS-1 of the Agreement, set forth in section 10 of the System Agreement, provides the mechanism by which each operating company makes or receives payments based on whether the capacity it owns exceeds, equals or is less than the system capability for which it is responsible. Schedule MSS-1 purportedly equalizes the system reserves borne by each operating company.

[23] *Id.*, at 23-24

[24] This issue is not reached as the FERC in this instance made a particular ruling that in spite of the fact that the payments were made in violation of a FERC approved tariff, no refunds were necessary.

21. Prior to August 5, 1997, in order to be counted as a part of a company's capability for determining MSS-1 payments, a generating unit had to be "available" for use by the system, as defined in Section 10.02(a) of the Agreement:

> A unit is considered available to the extent the capability can be demonstrated and (1) is under the control of the System Operator, or (2) is down for maintenance or nuclear refueling. A unit is considered unavailable if in the judgment of the Operating Committee it is of insufficient value in supplying system loads because of (1) obsolescence, (2) physical condition, (3) reliability, (4) operating cost, (5) start-up time required, or (6) lack of due-diligence in effecting repairs or nuclear refueling in the event of a scheduled or unscheduled outage.

22. Several years after the System Agreement was executed, on January 1, 1987, the Extended Reserve Shutdown ("ERS") Program was conceived, which allowed the operating companies to place generating units in an inactive status in order to reduce costs by reducing operating staff, maintenance costs, and deferring the costs of repairing units.

23. Since the inception of the ERS program, Entergy treated unqualified units in ERS status as if they were "available" within the meaning of Section 10.02 of the System Agreement, for purposes of calculating the Entergy Operating Companies' capability under MSS-1. [*Entergy Services, Inc. and Gulf States Utilities Company*, (Opinion No. 415), 80 FERC ¶61,197 (8/5/97) (Slip Op. at 3-5)]

24. Such treatment of ERS units benefits companies such as Arkansas Power & Light, while it results in increased MSS-1 payment obligations to companies such as ELI and Mississippi Power & Light. [*Id.*, at 8]

25. LPSC sought refunds of $19.4 million plus interest for the period January 1, 1987 through December 31, 1993, and additional refunds for the post-1993 period, because the treatment of ERS units as available increased ELI's MSS-1 payment obligations by that amount. [*Id.*] [25]

26. FERC Order No. 415, dated August 5, 1997 found that the treatment of ERS units as "available" was in violation of the System Agreement.

27. In spite of FERC's ruling that the treatment of ERS units as "available" was in violation the System Agreement, FERC denied the refunds sought by LPSC and MPSC [*Id.*, at 14]

28. FERC's jurisdiction under 16 U.S.C.A. §824(a) over interstate wholesale rate makes these system-wide concerns relevant to FERC, whereas in regulating retail rates, system-wide benefits are not a predominant factor is regulating retail rates.

29. The FERC found the "there was no unjust enrichment as a result of the violation, *given that Entergy as a whole received no net gain* from the inclusion of ERS units in Schedule MSS-1; . . . Entergy's actions resulted *in system-wide benefits in the form of enhanced system efficiencies and cost reductions* that ultimately benefited ratepayers . . ." [*Id.*, at 14-15, Emphasis provided].

30. FERC's conclusions were based on system-wide concerns and not on the effect of the violation on any individual operating company's retail rates.

31. In fact, those system-wide benefits which increase ELI's operation expenses show that other sister companies are benefiting from the MSS-1 treatment of ERS units at

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[25] Mississippi PSC was another party in the FERC proceeding which sought refunds.

ELI's expense; such system-wide benefits that adversely affect ELI indicate that ELI might have simply acquiesced in the parent company's decision without regard to the impact of such increased expenses on its ratepayers in Louisiana, and to its obligation to minimize its cost of providing service.

32. In Order No. 415-A dated February 3, 1998, FERC denied LPSC and MPSC's request for rehearing.

33. Order No. 415-A simply denied rehearing, and therefore no new hearings were conducted. Hence, Order No. 415-A contains no new findings of facts for the period August 5, 1997 through February 3, 1998. It simply reaffirms Order No. 415 dated August 5, 1997.

34. Under FERC Order Nos. 415 dated August 5, 1997 and 415-A dated February 3, 1998, ELI has an obligation to pay its sister companies higher MSS-1 payments resulting from treating ERS units as "available" within the meaning of Section 10.02 for the period January 1, 1987 to August 5, 1997.

35. There exists no FERC Order or other federal regulation that makes it mandatory for ELI to treat ERS units as available after August 5, 1997.

36. ELI was put on notice by FERC's Order No. 415 that the MSS-1 treatment of ERS units was in violation of System Agreement and that it resulted in significantly higher MSS-1 payments that ELI must pay its sister companies.

37. ELI did not consider the effect of increased MSS-1 payments on its retail rates in Louisiana when it decided to continue the MSS-1 treatment of ERS units.

38. ELI failed to minimize its operating costs when it decided to continue its treatment of ERS units after August 5, 1997.

39. ELI failed to property weigh the costs and benefits *to its retail customers* of treating ERS units as available.

40. ELI's duty to incur prudent costs and avoid imprudent costs includes the duty to follow the criteria set forth in the amended Section 10.02 in reaching a decision regarding the availability status of ERS units after August 5, 1997.

41. The Operating Committee, which made that decision, did not have complete or accurate information before it regarding the cost of bringing ERS units back to service.

42. At a meeting held in September 1997, Mr. Turner made a presentation to the Operating Committee with incomplete information contained in a single sheet of paper showing the estimated cost of return to service of the ERS units including capital investment and five year operation and maintenance costs on a net present value basis. [ELI Ex.. # 14. KMT Ex.. # 1, p.8 of 10]

43. Neither Mr. Turner nor his staff prepared any analyses of what it would cost to return the ERS units to service. [Tr. 2/16/98 at 101-103].

44. Mr. Turner is not an engineer, and he would not have been qualified to perform any of the analyses concerning the cost to return these units to service [Tr. 2/16/98 at 103].

45. At the time of the meeting when the Operating Committee made its decision based on Mr. Turner's presentation, Mr. Turner had not seen any analyses or studies concerning what it would cost to return the ERS units to service [Reply Brief at 12, citing Tr. 2/16/98 at 101].

46. Mr. Turner acknowledged that a study later conducted by Raytheon Engineers and Constructors, Inc. ("the Raytheon Study") was more detailed and reflected better

estimates of the cost of returning the ERS units to service. [Tr. 2/16/98, Confidential at 5].

47. In several instances the cost estimates in the Raytheon Study were more than twice as much as in the estimates provided by Turner to the Operating Committee [Tr. 2/16/98 Confidential at 3-4, and LPSC Staff Exhibit Nos. 6 and 7].

48. The Raytheon Study was not presented to the Operating Committee at its September 1997 meeting when it made the decision to classify these units as "available" [Tr. 2/16/98 at 106].

49. Mr. Turner could not give "a day, a week, a month, or even a year for any of these 24 [ERS] units . . . [or] a definite date when any of these units on this page [ERS units] will come out . . ." [Tr. 2/16/98 at 100].

50. Notwithstanding these admissions, Mr. Turner asserted that these units would be needed in the "relative near term", which he defined to mean "any time within the next 10 years." [Tr. 2/16/99 at 101].

51. The evidence does not show that the Operating Committee made necessary efforts to ascertain that ERS units would be needed within the next 10 years.

52. The evidence does not show that the Operating Committee made efforts to reach a decision "based on consideration of current and future resource needs, the projected length of time the unit would be in ERS status, projected cost of maintaining such unit, and the projected cost of returning the unit to service".

53. Those MSS-1 payments that were made subsequent to the FERC Order dated August 5, 1997, were also known to the utility, or should be known to the utility to be unreasonable and imprudent, at the time those expenses were incurred (i.e. subsequent to the FERC order dated August 5, 1997)

54. The MSS-1 overpayments for the test year of 1996 are extraordinary expenses that are not likely to be incurred prospectively, in view of FERC's finding that they are in violation of the System Agreement.

55. The MSS-1 overpayments made after August 5, 1997 were imprudently incurred.

Legal Analysis

In determining whether all or any portion of the payments made by ELI pursuant to MSS-1 should be excluded from the 1996 test year expenses, this Commission first resolved the following issues:

a. Is this Commission precluded by FERC Order No. 415 from assessing the reasonableness of the payments made by ELI in 1996 pursuant to a FERC approved tariff?

b. May this Commission determine whether the Operating Committee's decision was in compliance with the amended Section 10.02 of the System Agreement?

c. Is this Commission precluded from removing those overpayment expenses from the 1996 test year expanses for purposes of setting ELI's rates for the year 1997?

d. Does this Commission have authority to assess the prudence of ELI'S management decision to continue to include the ERS units in MSS-1 calculations *after* the August 5, 1997 FERC Order?

e. If so, did the Company act prudently in continuing to accord ERS units MSS-1 treatment?

f. Should this Commission find that management decision imprudent, may the Commission deny recovery of all or a prorated portion of MSS-1 payments for purposes of setting ELI's rates for 1997?

A resolution of these above issues depends upon a proper analysis of the respective jurisdictional and regulatory authority of the FERC and this Commission. Such an analysis warrants a review of the issues resolved in the FERC orders in question and also of the "filed rate doctrine" as expounded in the case law.

Preemption under the "filed rate doctrine"

Federal law may preempt state law in three ways: first, Congress may expressly define the extent to which it intends to preempt state law; second, Congress may only signal an intent to occupy the area; third, state laws that conflict with federal laws are preempted, even if Congress has not expressly preempted them or otherwise signaled its intent to occupy the area. U.S.C.A. Const. Art. VI, cl 2. Absent conflicting federal legislation, the states may exercise police power over matters of legitimate local concern even though such regulation may affect interstate commerce. *Philadelphia v. New Jersey*, 437 U.S. 617, 623-24, 98 S. Ct. 2531, 2535, 57 L.Ed.2d 475 (1978). Incidental burdens on interstate commerce may be unavoidable when a state legislates to protect its citizens. *Id.*

Under 16 U.S.C.A. §824(b)(1), the FERC has jurisdiction over all facilities for the sale of electric energy at wholesale in interstate commerce[26]; "sale of electric energy at wholesale in interstate commerce" is defined in §824(d) as "a sale of electric energy to any person for resale". FERC has exclusive jurisdiction to determine "just and reasonable" rates for wholesale sales of electric power in interstate commerce. 16 U.S.C.A. §824d(a). However, the Federal Power Act limits federal regulation of electric utilities engaged in interstate commerce "to those matters which are not subject to regulation by the States". 16 U.S.C.A §824(a).

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[26] This jurisdictional authority is subject to limited statutory exceptions as provided in §824(b)(2) which exceptions see not applicable here.

Thus, Congress has not explicitly stated, or even signaled an intent to occupy the field; in fact, FERC's authority is limited to those matters as specified in the FPA, and is limited "to those matters not subject to regulation by the States." §824(a). Thus, under the FPA, states' regulatory authority is preempted only where state regulation conflicts with federal regulation.

The U.S. Supreme Court confirmed this limited preemptive effect of the FPA, when it stated that the FPA "had no purpose or effect to cut down state power. On the contrary, perhaps its primary purpose was to aid in making state regulation effective". *Panhandle Eastern Pipe Line Co. v. Public Service Com'n of Indiana,* 332 U.S. 507, 517, 68 S.Ct. 190, 195, 92 L.Ed. 128. The Fifth Circuit similarly stated that it must be assumed that state police powers were not to be superseded by Federal Power Act in the absence of clear and manifest congressional purpose. Federal Power Act §§321 et seq., as amended 16 U.S.C.A §§792 et seq., 791a, U.S.C.A. Const. Art. VI cl.2. *New Orleans Public Service, Inc., v. Counsel of City of New Orleans*, 911 F.2d 993, rehearing denied, certiorari granted 111 S.Ct 1617, 499 U.S. 974, 114 L.Ed.2d 715, certiorari dismissed 112 S.Ct 411, 502 U.S. 954, 116 L.Ed.2d 357.

In determining whether a state's regulation conflicts with FERC's authority, courts have used the "filed rate doctrine", stated as follows: In interpreting the extent of FERC's authority under this statutory grant of jurisdictional and regulatory power, "the right to a reasonable rate is the right to the rate which the [Federal Energy Regulatory] Commission files or fixes, and, . . . except for review of the Commission's orders, [a] court can assume no right to a different one on the ground that, in its opinion, it is the only or the more reasonable one." *Montana-Dakota Utilities Co. v. Northwestern Public Service Co.*, 341 U.S. 246, 251-252, 71 S.Ct. 692, 645, 95 L. Ed. 912 (1951).

In *Nantahala Power & Light Co. v. Thornburg*, 476 U.S. 953, 106 S.Ct. 2349, 90 L.Ed.2d 943 (1986) the Court held that the filed rate doctrine precluded the State of North Caroline from setting retail rates that did not take into account FERC's allocation of power between two related utility companies; and similarly in *Mississippi Power & Light v. Mississippi Ex Rel. Moore*, 487 U.S. 354, 108 S.Ct. 2428, 101 L.Ed.2d 322, relying on *Nantahala*, the Court reversed a ruling by the Mississippi Supreme Court that FERC's allocation of a 33% share of the costs associated with a nuclear power plant to MP&L did not obligate the State to approve a pass-through of those costs to state consumers without a prudence review. In *Mississippi Power & Light, supra*, the Court stated:

> . . . States may not alter FERC-ordered allocations of power by substituting their own determinations of what would be just and fair. FERC-mandated allocations of power are binding on the States, and States must treat those allocations as fair and reasonable when determining retail rates.

Our decision in *Nantahala* relied on fundamental principles concerning the preemptive impact of federal jurisdiction over wholesaler rates on state regulation. First FERC has exclusive authority to determine the reasonableness of wholesale rates. . . . [The filed rate doctrine] binds both state and federal courts and is in the former respect mandated by the Supremacy Clause. 476 U.S., at 963, 106 S.Ct., at 2355. Second, FERC's exclusive jurisdiction applies not only to rates but also to power allocations that affect wholesale rates. *Id.*, at 966, 106 S.Ct., at 2356-2357. Third, States may not bar regulated utilities from passing through to retail consumers FERC-mandated wholesale rates. "The filed rate doctrine ensures that sellers of wholesale power governed by FERC can recover the costs incurred by

> their payment of just and reasonable FERC-set rates. When FERC sets a rate between a seller and a wholesaler-as-buyer, a State may not exercise its undoubted jurisdiction over retail sales to prevent the wholesaler-as-seller from recovering the costs of paying the FERC-approved rate . . . Such a 'trapping' of costs is prohibited."

Id., at 974, 106 S.Ct. at 2359.

Thus, the filed rate doctrine restricts state regulation of the electric utility industry in that, in regulating retail rates, states may not challenge federally approved wholesale rates as unreasonable, thereby "trapping" the federally approved costs incurred by the utility. This principle set forth in *Mississippi Power & Light* and *Nantahala* has been followed in several state court decisions. For example, in *Narragansett Electric Co. v. Burke*, 119 R.I. 559, 381 A.2d 1358 (1977), *cert denied*, 435 U.S, 972, 98 S.Ct. 1614, 56 L.Ed.2d 63, the Rhode Island Supreme Court held that the state regulatory commission could not review the reasonableness of FERC-approved wholesale rates and must treat the FERC rates as reasonable operating expenses when establishing a utility's costs of retail service. *Id.*, at 1363.

The Pike exception

An exception to the pre-emptive force of the filed rate doctrine, as enunciated in *Montana-Dakota Utilities, Inc.*, was crafted by a Pennsylvania court in *Pike County Light and Power Co. v. Pennsylvania Public Utility Commission*, 77 Pa. Cmwlth. 268, 463 A.2d 735 (1983), where it was held that despite FERC's exclusive jurisdiction to set just and reasonable rates, FERC "makes no determination of whether to *incur* such a rate as an expense." *Id.* 465 A.2d at 738. [Emphasis in original.] The *Pike* court reasoned that, while FERC has exclusive statutory jurisdiction under the FPA to set just and reasonable rates, a determination of the prudence

of the purchaser's decision to purchase power from this source is not exclusively within FERC's jurisdiction. Therefore, the court concluded, the filed rate doctrine does not limit the jurisdictional and regulatory authority of a state commission to review a utility's decision to purchase power at a higher (albeit FERC-approved) price, where there are alternative sources of power at a lower price than the FERC-approved price.

In *Nantahala*, the Court expressly acknowledged the *Pike* exception when it noted that in certain circumstances, a utility's purchase of a particular quantity of high cost power at FERC-approved rates might be unreasonable, if lower cost power were available from another source. *Nantahala*, 476 U.S. at 972, 106 S.Ct. at 2359, quoting from *Pike*. The Court determined, however, that this line of cases had no application where FERC has not only determined the (wholesale) rate but also the source and/or quantity of power to be purchased.[27]

The U.S. Supreme Court indirectly addressed this issue (in the context of the proper exercise of *Burford/Younger* abstention by a federal court) in *New Orleans Public Service, Inc., v. The Council of the City of New Orleans, et al.*, 491 U.S. 350, 109 S.Ct. 2506, 105 L.Ed.2d 298 (1989). Though the Court did not address the specific issue of whether the review by the Council of New Orleans (the local regulatory body) of NOPSI's prudence in a decision made subsequent to a FERC order violated the filed rate doctrine, the Court remanded the case, noting specifically that:

> The Council has not sought directly to regulate interstate wholesale rates; nor has it questioned the validity of the

[27] Of course, under *Pike*, even where the FERC mandates the quantity and/or source of power to be purchased, States will have jurisdiction to review the prudence of a utility's action where the quantity purchased exceeds that mandated by the FERC.

> FERC-prescribed allocation of power within the Grand Gulf system, or the FERC-prescribed wholesale rates; nor has it reexamined the prudence of NOPSI's agreements to participate in Grand Gulf 1 in the first place. Rather, the Council maintains that it has examined the prudence of NOPSI's failure, after the risks of nuclear power became apparent, to diversify its supply portfolio, and that finding that failure negligent, it has taken the normal rate-making steps of making NOPSI's shareholders rather than the ratepayers bear the consequences. Nothing in this is directly or even indirectly forclosed by the federal statute, the regulations implementing it, or the case law applying it.

Id., at 367, 109 U.S. 2518.

On remand, the Fifth Circuit, in *New Orleans Public Service, Inc., v. The Council of the City of New Orleans, et al*, 911 F.2d 993 (5th Cir. 1990), held that the filed rate doctrine did not preclude the Council from examining NOPSI's prudence in not acting to minimize its losses. The court's conclusion was based on its findings that the FERC did not assert jurisdiction to determine NOPSI's prudence in its lack of efforts to minimize its total cost exposure for the Grand Gulf project, and that the Council's resolution specifically provided that, in determining the appropriate retail rate increase, the Council would not seek to invalidate any of the agreements surrounding Grand Gulf 1 or to order NOPSI to pay the seller a wholesale rate other than that approved by FERC.

Several state courts and regulatory bodies have followed the reasoning in *Pike* and in the *NOPSI* cases, in allowing the State regulatory bodies this limited area of prudence review where the actions examined are not covered by the FERC resolution. *See Re FERC Order 636 Transition Costs*, 93-0328, Illinois Commerce Commission, 150 PUR 4th 181; *Alliance for Affordable Energy v. New Orleans*, 578 So.2d

949 (La.App. 4 Cir. 1991)[28]; and denying such authority where the particular action examined by the State regulatory agency has already been approved or mandated by FERC. E.g., *General Motors Corporation v. Illinois Commerce Commission*, 574 N.E.2d 650 (Ill. 1991); *Connecticut Light and Power Company v. Connecticut Department of Public Utility Control, et al.*, 148 PUR 4th 364 (Connecticut Superior Court, 1993); *Re Final Statement of Policy Regarding Recovery of Tare-or-pay Expenses*, 104 PUR4th 185 (1989); *Re Interstate Power Co.*, 103 PUR 4th 177 (1989); *Re Pennsylvania Power Co.*, 93 PUR 4th 359 (1988); *Re Costs Associated with Take-or-pay Charges*, 95 PUR 4th 5 (1988); *Kentucky West Virginia Gas Co. v. Pennsylvania Pub. Utilities Commission*, 837 F.2d 600 (3d Cir. 1988).

The Pike-exception has thus carved out a limited area where the filed rate doctrine or the supremacy clause does not deprive the States of their authority to examine the prudence of a regulated utility's actions, where such actions are not *mandated* by federal regulation (such as a FERC order or tariff), but are left to the discretion of the utility. Thus, a proper application of the *Pike* exception depends on whether the particular action of the utility scrutinized by the State regulatory body for reasonableness and prudence has already been approved/ mandated by FERC or whether it has been left to the discretion of the utility by FERC.

Application of the Law:

a. Is this Commission precluded from assessing the reasonableness of the MSS-1 payments made by ELI for the year 1996 pursuit to FERC Order No. 415?

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[28] On appeal, after a writ of certiorari was granted by the Louisiana Supreme Court, this case was vacated by the Supreme Court by virtue of a Consent Decree that was entered into by all parties. *Alliance for Affordable Energy v. The Council of the City of New Orleans*, 588 So.2d 89 (La. 1991). The merits of the decision by the 4th Circuit were not disturbed as the case was vacated upon a Joint Motion by all parties.

The instant case does not present one of the necessary elements of the filed rate doctrine, to wit, "FERC-approved or FERC-set rates", because the FERC indeed found that the inclusion of ERS units in MSS-1 calculation was in violation of Schedule MSS-1 of the System Agreement. Hence, this case can be distinguished from all the cases discussed above. This Commission's review of the case law on the filed rate doctrine has not disclosed any case where a State Commission was faced with the issue of a FERC finding that expenses have been incurred in violation of a FERC tariff. Nor have the parties cited any case addressing issues presented by such a factual situation. This issue therefore remains an open question.

However, in Order No. 415, FERC also found that the overpayments made by ELI as result of such a violation "did not result in an unjust, unreasonable or unduly discriminatory outcome in the circumstances". In other words, in a seemingly paradoxical manner, FERC has approved the results of what it found to be a violation of a FERC tariff. The FERC Order also approved the amendment to Section 10.02 of the System Agreement, which according to FERC, would sufficiently safeguard against future violations through continued inclusions of ERS units in MSS-1 calculations. The original FERC Order was dated August 5, 1997, and the Order denying rehearing, February 1998. ELI states that the amendment to Section 10.02 became effective August 5, 1997.[29] [ELI's Post-Hearing Reply Brief at 23-24]

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[29] The FERC Order, however, provides that, "Schedule MSS-1 is hereby amended, *effective as of the beginning of the first complete billing cycle following the date of issuance of this order*, to clarify the treatment of ERS units as provided in the Offer of Settlement." [Emphasis provided]. The parties have not introduced any evidence concerning when the first billing cycle following the issuance of FERC Order No. 415 began, nor has ELI suggested any effective date other than August 5, 1997, the date of that FERC Order.

Under 16 U.S.C.A. §824e(a), FERC has exclusive authority to determine whether "any . . . contract affecting such rate, charge, or classification is unjust, unreasonable, unduly discriminatory or preferential . . ."; and under §824e(b) "the [FER] Commission may order the public utility to make refunds of any amounts paid . . . is excess of those which would have been paid under the just and reasonable rate, charge, . . . price of contract which the Commission orders to be thereafter observed and in force." In Order No. 415-A, the FERC explains that it has discretion in ordering refunds, which it exercised in Order No. 415 in rejecting claims for refund by appellants, including the LPSC. Therefore, under *Mississippi Power & Light* and *Nantahala*, this Commission lacks authority to review the reasonableness of ELI's 1996 MSS-1 overpayments or to order refunds of the same, contrary to FERC's express refusal to order such refunds imposing an obligation on ELI to make those payments. Such an inquiry by this Commission would violate the filed rate doctrine, supremacy clause and principles of *res judicata*, as ELI points out.

b. Is this Commission precluded from determining whether the Operating Committee's decision was in compliance with the amended Section 10.02 of the System Agreement?

LPSC Staff argues that the MSS-1 overpayments should be disallowed in this proceeding because the Operating Committee's decision violates the amended Section 10.02 of the System Agreement, a tariff filed with the FERC. Special Counsel thus invites this Commission to adjudicate the issue of whether ELI has violated a FERC-filed tariff. As ELI argues in its Post-Hearing and Reply briefs, this Commission is pre-empted from determining whether the terms of a FERC tariff have been met, for the issue of violation of or compliance with a FERC tariff is peculiarly within FERC's purview. Any allegation of a violation of a FERC-tariff should therefore be brought before the FERC.

However, (as will be discussed in the following subsections), if this Commission is not precluded from reviewing the *prudence* of the Operating Committee's decision to incur increased costs due to the treatment of units in ERS status, and should it find that decision imprudent, then it can disallow those increased costs resulting from such decision. In doing so, this Commission will not interfere with FERC's authority to judge Entergy's actions under the System Agreement, because, as will be discussed in detail below, FERC Order No. 415 dated August 5, 1997 does not address the reasonableness of ELI's actions subsequent to that date. Therefore, though FERC has exclusive jurisdiction over the issue of whether the System Agreement has been violated, there currently exists no FERC order that has found that the Operating Committee's decision is in compliance with the System Agreement. In the absence of such FERC determination, this Commission can scrutinize the prudence of the Operating Committee's decision without violating the supremacy clause insofar as that decision affects retail rates. (This Commission's authority to scrutinize ELI's decision to continue to accord MSS-1 treatment to ERS units will be discussed in the following subsections.)

This Commission also finds that in determining the prudence of ELI's decision subsequent to August 5, 1997, this Commission is neither limited to the criteria set forth in the amended Section 10.02, nor does it have to necessarily abstain from using those FERC-set criteria in examining ELI's actions. In addition to the well-established standards for judging prudence such as reasonableness, economy, impact on retail rates, duty to minimize cost of service, duty to avoid risk, etc., this Commission can also take judicial notice of the FERC-set standard for treating ERS units as available. ELI's duty, as a regulated utility, to incur prudent costs and avoid imprudent costs includes the duty to follow the criteria set forth in the amended Section 10.02 in reaching a decision regarding the availability status of ERS units after

August 5, 1997. Thus, the amended Section 10.02 may serve as an additional test for reasonableness and prudence in this Commission's review of ELI's MSS-1 expenses.

c. Is this Commission precluded from removing from the 1996 test year expenses the MSS-1 overpayments for purposes of setting ELI's 1997 rates?

ELI agues that removal of the MSS-1 overpayments for the 1996 test year in setting ELI's 1997 rates amounts to an order by Commission ordering refunds of those 1996 MSS-1 overpayments, and would constitute the prohibited "trapping" under *Mississippi Power & Light, supra.* [ELI Post-Trial Brief at 32, referring to Catlin's testimony].

However, FERC's Order No. 415 only addressed the issue of *refunds* of those overpayments, whereas rate-making is, by definition, *prospective. Bristol & Warren Gas Co. v. Burke*, 439 A.2d 246 (R.I. Sup. Ct 1981). There are two aspects of the issue currently before this Commission that FERC did not address or resolve, and those aspects are not foreclosed by the filed rate doctrine and the supremacy clause: (1) the validity of including MSS-1 payments made in 1996 in the calculation of test year expenses for purposes of setting rates for the year 1997-1998 (not for purposes of determining recovery of those very expenses incurred in the year 1996 via rates for 1996-1991); [30] and (2) subsequent to the FERC's pronouncement that the inclusion of ERS units in MSS-1 calculations was in violation of the System Agreement, the prudence of ELI's management decision to continue to incur the increased expenses of MSS-1 payments resulting from the inclusion of ERS units in calculating system capacity.

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[30] The rate-effective period for the implementation of the rates established in this proceeding, i.e. 1997 FRP, is July 1, 1997 through June 31, 1998. See the discussion on the rate-effective period provision under the FRP Rider under the section ALJ Rulings on Exceptions to the Proposed Recommendation, and footnotes 1-3 in that section.

With regard to the first issue (i.e. the validity of the inclusion of the MSS-1 payments made in violation of the FERC tariff as part of the test year expenses in setting rates for 1997-1998), though this Commission is bound by FERC's finding that the violation of the System Agreement did not warrant refunds, FERC's *did not order, prospectively*, that ELI and the other sister companies must continue to include ERS units in MSS-1 calculations, or that payments resulting from such continued inclusion are just and reasonable. To the contrary, FERC found that previous inclusion of ERS units under MSS-1 was in violation of the FERC-approved tariff, stated that the Company's discretion was not unfettered, and amended the tariff to provide some direction.

Thus, this Commission by the authority to disallow, for purposes of prospectively setting the rates for the year 1997-1998, the test year expenses of MSS-1 overpayments that FERC found were made in violation of the tariff, contrary to ELI's argument that post-test-year events may not be reflected in the calculation of test year expenses. (ELI's Reply Brief at 23-24). Such an adjustment to the test year is encompassed by the principles of "known and measurable" pro forma adjustments, and the exclusion of extraordinary or unusual expenses from test year expenses:

> Only prudent and efficient costs should be charged to the consumer. In other words, the consumer is responsible for the lowest cost of providing reasonable service, and no more. And the Commission is responsible for seeing that the consumer does not pay more. . . . . .
>
> The cost of service determined by a commission is to be representative of the conditions that will prevail when the rates will be effective; i.e., rate making is prospective. As a result, *pro forma* adjustments are made to the test year actual costs to represent more accurately prospective conditions.

> Another type of *pro forma* adjustment includes adjustments for abnormal and extraordinary revenues or costs. Abnormal levels of revenues and costs may be changed to normal levels. . . . To determine prospective rates, normal levels of sales, revenues, and costs would be included in the cost of service. Extraordinary costs are removed from the cost of service when costs are unlikely to be incurred prospectively. . . . To incorporate extraordinary costs would generate revenues unneeded in the future to cover actual costs incurred; a windfall profit would occur, a windfall profit not needed to cover costs.

Howe, Keith M. And Eugene F. Rasmussen, *Public Utility Economics and Finance*. Prentice-Hall, New Jersey, 1982, p. 74-75.

Contrary to ELI's assertion, post-test year adjustments to exclude non-recurring and unusual expenses from test-year operating expenses are encountered routinely in rate cases. e.g., *Re Idaho Power Co.*, 76 PUR 4th 326 (1986) (exclusion of computer lease cancellation payments from utility's test-year operating expenses as non-recurring); *Iowa-Illinois Gas & E. Co.*, 68 PUR4th 115 (1985) (post-test-year adjustment of expanses to reflect known and measurable changes in wages and medical insurance premiums); *Re Central Vermont Public Service Corporation*, 113 PUR4th 220 (1990) (prospective adjustment of prices of output and resources to reflect a known and measurable change); *In re: Annual monitoring of Gulf States Utilities Company's Louisiana jurisdictional revenue requirement study under terms of the Joint Regulatory Proposal set forth in Appendix 1 to Commission Order No. U-19904*, Louisiana Public Service Commission, Order No. U-22092 (adjustment of test-year cost savings expenditures which were found to be nonrecurring).

In this case, the MSS-1 payments made in violation of the FERC are unlikely to be incurred prospectively, especially

after FERC's own finding that MSS-1 treatment of ERS units is a violation of the tariff which increased ELI's MSS-1 expenses. Those MSS-1 payments that were made subsequent to the FERC Order dated August 5, 1997 were also known to the utility, or should be known to the utility to be unreasonable and imprudent, at the time those expenses were incurred (i.e. subsequent to the FERC order dated August 5, 1997). Thus, this Commission's decision to adjust the 1996 test year expenses to exclude the overpayments resulting from the MSS-1 treatment accorded to ERS units is consistent with the regulatory principles of adjusting for extraordinary and unusual expanses and for known and measurable changes in conditions that more accurately reflect the conditions that will prevail through the rate-effective period.

An adjustment by this Commission for extraordinary or imprudent expenses, so long as such adjustment does not make dual compliance impossible, would not violate the filed rate doctrine or the supremacy clause. It is also not *res judicata* since no determination was made by the FERC as to the prospective reasonableness of ELI's violation.

d. Does this Commission have authority to assess the prudence of ELI's management decision to continue to accord MSS-1 treatment to ERS units after August 5, 1997?

A court or agency must assume that state police powers were not to be superseded by Federal Power Act in the absence of clear and manifest congressional purpose. Federal Power Act §§321 et seq., as amended 16 U.S.C.A. §§792 et seq., 791a; U.S.C.A. Const. art. VI, cl.2. *New Orleans Public Service, Inc., v. Council of City of New Orleans*, 911 F.2d 993, rehearing denied, certiorari granted 111 S.Ct. 1617, 499 U.S. 974, 114 L.Ed.2d 715, certiorari dismissed 112 S.Ct. 411, 502 U.S. 954, 116 L.Ed.2d 357. It must also presume that state law is not pre-empted, as this is an area traditionally regulated by the states under their historic police power. *California v. ARC America Corp.*, 490 U.S. 93, 109 S.Ct.

1661, 104 L.Ed.2d 86 (1989). Congress' acknowledgment of States' authority over retail rates is expressly stated in §824(a). Thus, to the extent that this Commission's decision does not conflict with FERC orders or make dual compliance impossible, this Commission has the authority to review the prudence of ELI's actions *after* August 5, 1997 what no federal regulation existed that made MSS-1 overpayments mandatory. Such a prudence review would also not violate the supremacy clause. "[T]he regulation of utilities is one of the most important of the functions traditionally associated with the police power of the states." *Arkansas Electric Cooperative Corp. v. Arkansas PSC*, 461 U.S. 375, 377, 103 S. Ct. 1905, 1908, 76 L. Ed.2d. 1 (1983).

In Order No. 415, FERC only declined to order refund of amounts paid in violation of the tariff, and did not reach the issue of ELI'S prudence in *continuing to treat* ERS units as available. Thus, the extent of the FERC order stops at refusing to order refunds and approving the amendment to Section 10.02; FERC simply did not rule on the issue of whether ELI's decision to continue to include ERS units in MSS-1 calculations is a prudent one, and whether ELI must continue to make overpayments to its sister companies that the FERC found to be in violation of the System Agreement though no refunds were ordered. FERC's order did not make any future inclusion of ERS units in MSS-1 calculation mandatory. Thus, ELI had the option of continuing to treat ERS units as available upon meeting the criteria set forth in the amended Section 10.02, or treating them as unavailable. ELI was put on notice by the FERC decision that the inclusion of ERS Units in MSS-1 calculations would result in increased operating costs for ELI. Thus, (as is *NOPSI*), ELI's management decision to *continue to include ERS units in MSS-1 calculations after August 5, 1997, with the awareness that such treatment costs more to ELI, and benefits some other operating companies*, having never been addressed or decided by the FERC, was obviously not mandated by the

FERC order. This Commission as the retail ratemaking authority, has jurisdiction to decide that issue.

ELI argues that the FERC's order No. 415-A (denying rehearing) addresses the reasonableness of payments made *up to February 3, 1998*. [ELI, Post-Trial Brief at 26, 31]. However, a review of Order No. 415-A shows that the February. 1998 Order simply denied rehearing. Needless to say, no new hearings were held, no new findings of facts made in the February 1998 Order No. 415-A, and no new determinations of reasonableness were made by FERC, of MSS-1 treatment of ERS units for the period starting from August 5, 1997 to February 3, 1998. ELI has not directed this Commission to any evidence in support of its assertion that the MSS-1 payments made up to February 3, 1998 are shielded from a review by this Commission. This Commission finds no evidence to show that ELI's obligation to make MSS-1 payments under Order No. 415 was extended by Order No. 415-A to February 3, 1998. In fact, Order No. 415-A reaffirmed FERC's prior approval of the amendment to Section 10.02. Thus, ELI's obligations to make MSS-1 payments for the period ending August 5, 1997 were governed by Order No. 415, and its obligations subsequent to that period, as confirmed by Order No. 415-A, were governed by the amended Section 10.02 of the System Agreement. ELI's obligations to make FERC-approved overpayments ceased on August 5, 1997. As FERC made no attempt to assert jurisdiction over the question of ELI's prudence in continuing to accord ERS units MSS-1 treatment subsequent to the amendment of Section 10.02 of the System Agreement, ELI's arguments of *res judicata* and pre-emption have no application.

Thus, FERC's decision refusing to order a refund, only bound ELI to make MSS-1 payments to its sister companies, including the additional amounts resulting from treating ERS units as "available" up to the date of the FERC order, i.e.

August 5, 1997. *ELI was not under a FERC mandate to continue to accord ERS units MSS-1 treatment or to continue to make payments resulting from such treatment. To the contrary, ELI has been put on notice that their past treatment was in violation of the FERC tariff, and according to FERC, the approved amendment required different conduct before according such treatment.*

The principles enunciated in *Pike* and its progeny, *NOPSI v. Council for the City of New Orleans, supra*, in particular, support such a review by this Commission; this Commission a not interfering with the FERC order which denied refunds, for no refunds are ordered by this Commission; this Commission is similarly not challenging FERC's finding that Entergy's violation did not result in unjust, unreasonable, or unduly discriminatory outcome, for no inquiry into the reasonableness of the payments made up to the date of the FERC order (August 5, 1997) is made by this Commission. Finally, this Commission is not assessing Entergy's compliance with the amended Section 10.02 of the System Agreement, for a determination of violation or compliance with a FERC tariff is peculiarly within FERC's purview. (However, that question of whether the continued inclusion of ERS units in MSS-1 calculations complies with the amended Section 10.02 has never been addressed or decided by the FERC, and therefore no FERC order exists, with which this Commission's finding of imprudence could conflict.)

This Commission merely examines the prudence of ELI's management decision to continue, *after* August 5, 1997, to include ERS units in MSS-1 calculations, once the increased costs of such treatment to ELI and its ratepayers is evident to ELI, and such a treatment is not mandated by the FERC order. Such a prudence review, as explained above, is not preempted by the filed rate doctrine, and does not violate the supremacy clause, and is not *res judicata*.

e. Did ELI act prudently in continuing to accord ERS units MSS-1 treatment?

Pursuant to its authority as a retail ratemaking body, as explained above, this Commission now addresses the prudence of ELI's decision to continue to accord MSS-1 status to ERS units after August 5, 1997, and finds that decision was neither prudent nor reasonable, based on the following facts:

FERC's own finding that Entergy's treatment of ERS units violated the System Agreement, and resulted in increasing operation expenses to ELI and EMI shows that ELI was made aware by the FERC order of the increased costs to ELI and its ratepayers, if it was not aware of that prior to that date. Similarly, the evidence in this proceeding shows that ELI was not prudent in minimizing its MSS-1 payment expenses once it was no longer mandated by a FERC order to make those overpayments to its sister companies.

The FERC found that "there was no unjust enrichment as a result of the violation, *given that Entergy as a whole received no net gain* from the inclusion of ERS units in Schedule MSS-1 . . . Entergy's actions resulted *in system-wide benefits, in the form of enhanced system efficiencies and cost reductions* that ultimately benefited ratepayers . . ." (FERC Order No. 415 at 14-15, Emphasis provided]. These findings, as reflected in the italicized portions of the FERC order, apply *at the level of the parent company*, whereas this Commission is concerned solely with ELI in this proceeding. FERC's jurisdiction under 16 U.S.C.A §824 over interstate wholesale makes system-wide concerns relevant to FERC, whereas in regulating retail rates, system-wide benefits are not of prime importance to a state Commission.

In fact, where those system-wide benefits increase ELI's operation expenses, it is a reflection of the utility's failure to exercise its discretion to limit expenses, and of its

acquiescence in the parent company's decision without regard to the impact of such increased expenses on ELI's ratepayers. The impact of MSS-1 expenses on retail rates guides this Commission's review of ELI's actions insofar as the utility is not obligated to incur those expenses under the FERC order. ELI's actions affect its ratepayers in Louisiana, and this Commission's authority to regulate retail rates without interfering with FERC-set wholesale rates includes the authority to examine the prudence of ELI's management decision that affects the retail rates in Louisiana.

In addition, ELI's obligation to incur prudent costs and avoid imprudent costs includes the obligation to follow the criteria set forth in the amended Section 10.02 in reaching a decision regarding the availability status of ERS units after August 5, 1997. The Operating Committee, which made the decision, did not exert due diligence in ascertaining the costs and benefits of bringing ERS units back to service. The information presented to the Operating Committee was not based on any study of such relative costs and benefits; the Raytheon study, which the parties agree was more detailed and contained more accurate estimates, was not available to the Operating Committee at the time it made the decision under review; the estimates in the Raytheon study were sometimes more than twice the amounts reflected in Mr. Turner's presentation to the Operating Committee. The evidence does not show that the Operating Committee made efforts necessary to ascertain that ERS units would be needed within the next 10 years. The Operating Committee did not even seek the information necessary to reach a well-considered decision. The evidence shows that the Operating Committee failed to obtain the requisite data in order to reach a decision "based on consideration of current and future resource needs, the projected length of time the unit would be in ERS status, projected cost of maintaining such unit, and the projected cost of returning the unit to service".

When its obligation to make the higher MSS-1 payments ceased on August 5, 1997, ELI should have responded with a more thorough evaluation of that change in circumstances in an attempt to minimize its cost of service. Inquiry under the prudent investment rule encompasses the public utility's continuation of a plan, as well as its decision to enter into that plan, and requires the utility to respond prudently to changes in circumstances and new challenges that arise. *Gulf States Utilites v. LPSC,* 578 So.2d. 71 (La. 1991), rehearing denied, certiorari denied 112 S.Ct 637, 502 U.S. 1004, 116 L.Ed.2.d 655.

Therefore, this Commission's authority to review ELI's decision regarding ERS units after August 5, 1997 is not preempted by FERC orders No. 415 and 415-A. As in *NOPSI, Pike*, and the numerous cases that have followed them, the utility's action that is being reviewed by this state commission (i.e. continuation of MSS-1 treatment of ERS units after August 5, 1997) was not mandated by FERC. Rather, the utility had a opportunity to make a different decision and minimize its costs. Again, as in *NOPSI* and *Pike*, it is the prudence of that decision not to minimize costs that is being reviewed by this state commission. Indeed, this case presents stronger facts than *NOPSI* and *Pike,* in that the Company was put on notice by the FERC order that it was incurring increased costs, and the Company decided to continue a decision that FERC had found to be in violation of a FERC tariff.

Based on these facts, this Commission concludes that ELI acted imprudently in not minimizing its MSS-1 payments after August 5, 1997 when its FERC-set obligations to make those payments ceased. Therefore, ELI's MSS-1 overpayments for the test year of 1996 should be removed in setting its 1997-1998 rates. (However, as will be explained below, those excess payments cannot be completely disallowed since

the company's obligations under the FERC order extend partially into the rate-effective period starting July 1, 1997.)

f. Should this Commission find ELI's treatment of ERS units imprudent, does it have the authority to deny recovery of all of a prorated portion of MSS-1 payments for purposes of setting ELI's rates for 1997?

ELI argues that post test–year events may not be reflected in the calculation of test year expenses. However, this general principle that ELI relies on is subject to well-defined exceptions established by traditional regulatory priniciples such as "known and measurable" pro forma adjustments to the test year expenses, as explained above. Such adjustment in this case cannot bar MSS-1 overpayments for the whole of the rate-effective period that started on July 1, 1997, because of the FERC order refusing to order refunds of overpayments made up to August 5, 1997, the date of that Order. If the FERC Order had been issued on June 31, 1997, this Commission could adjust the 1996 test year expenses to completely exclude MSS-1 overpayments. However, the FERC order was issued on August 5, 1997, which denied refunds of all overpayments made up to that date, making it mandatory for ELI to make those payments to its sister companies.[31] Hence, this Commission cannot adjust the test year expenses to completely exclude 1996 MSS-1 payments without interfering with FERC-set wholesale rates, without "trapping" a FERC-approved overpayment. Therefore, the adjustment to the test year expenses has to be prorated in a manner such that overpayments that ELI is obligated to make

[31] As discussed in a previous section, ELI's argument that FERC's finding of reasonableness shields MSS-1 payments made up to February 3, 1998 (the date of issuance of Order No. 415-A) is rejected because Order No. 415-A simply reaffirmed the prior order dated August 5, 1997 and made no new findings of fact concerning the period between the two orders.

under the FERC order (i.e. up to August 5, 1997) will not be disallowed by this Commission in contravention of the supremacy clause and principle of *res judicata*. Hence, this Commission orders that all MSS-1 overpayments incurred on or after August 6, 1997 be removed from the company's calculation of its cost of service and credited back to the ratepayers.

Conclusion

This Commission has the authority to assess the prudence of ELI's decision to contiune to accord MSS-1 treatment to ERS units subsequent to FERC order No. 415 dated August 5, 1997. This Commission finds that the evidence in this proceeding shows that decision by ELI's management did not consider the negative impact on ELI's retail rates, and its decision was not based on accurate or complete information. This Commission also finds that ELI failed to minimize its operating costs when it decided to continue to accord MSS-1 treatment to ERS units after August 5, 1997, as the Company was put on notice by FERC Order No. 415 that such a treatment resulted in increased costs to ELI, and was in violation of the System Agreement. This Commission also finds that ELI did not take the necessary steps to obtain the information that the amended Section 10.02 requires it to, and hence it failed in its obligation to make a well-considered decision. The Company's imprudent decision has an adverse effect on its retail rates in Louisiana. The increased MSS-1 payments resulting from the treatment of ERS units as available under Schedule MSS-1 in violation of a FERC tariff should be removed from the company's calculation of its cost of service, but such disallowance should be prorated because FERC Order No. 415 imposed an obligation on ELI to make those payments for a part of the rate effective period (i.e., up to August 5, 1997).

This prorated disallowance does not create a conflict between federal and state law that would render dual compliance impossible. ELI could accept the FERC MSS-1 payments under Order No. 415 dated August 5, 1997 and still not recover continued MSS-1 overpayments past that date—i.e. ELI's ability to pay its FERC-mandated MSS-1 costs is not affected by this Order. The FERC set the MSS-1 payment levels affecting ELI's wholesale rate up to August 5, 1997. This Commission's Order sets ELI's retail rates for the rate effective period, 1997-1998, disallowing overpayments only after August 5, 1997, the date when ELI's obligation to make the FERC-mandated payments ceased.

3. RATE CAP ISSUE

Background

Under the rate cap provision in Order No. U-20925, implementing the Formula Rate Plan, ELI is subject to a base rate cap equivalent to its base rates as of December 31, 1994. This rate cap provision was recommended by LEUG in ELI's 1994 rate review proceeding. However, the FRP Rider filed by ELI to implement the FRP changes the wording to read revenue cap. LEUG filed comments with the Commission to bring to the Commission's attention the variation between term "revenue cap" in ELI's FRP Rider and the term "rate cap" in Order No. U-20925. LEUG contended that the term "revenue cap" could possibly be interpreted to require only that ELI's total revenues, and not individual rates, be maintained at or below the December 31, 1994 levels, and arguably would allow ELI to increase some its rates above the December 31, 1994 levels so long as there are decreases in other rates that would keep the company's total revenues constant within a twelve month period. LEUG argued that the term "revenue cap", interpreted in such a manner, allows the company to defeat the Commission's purpose of a rate cap ordered by the Commission to ensure rate stability.

LEUG raised this issue in the First FRP Review, and testimony was filed by both LEUG and ELI on the issue and related issues. The Administrative Law Judge's recommendation, in that proceeding, dated January 12, 1998, stated that the issue was not ripe for a determination as no rate increase was proposed by ELI at that time. LEUG presented an oral argument on this issue at the Commission's January 21, 1998 B&E meeting. The Commission decided that it was not ready to make a determination on this issue when no rate increase proposed by ELI was before the Commission. However, the Commission expressed a desire that the rate cap issue be addressed in one of the upcoming proceedings involving ELI, such as the second FRP.[32]

On September 5, 1996, ELI filed an Application for Authorization to Implement a New Rate Plan ("Application") which was originally docketed as U-22137. Contained in the Application, through the testimony and exhibits of Dr. John H. Chamberlin[33] was the Company's request to restructure its standby rate tariff.[34]

On February 9, 1998, LEUG filed a Motion to Transfer Testimony that was previously filed into record in the first FRP proceeding in Docket No. U-20925 on the issue of rate

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[32] January 21, 1998 B&E at p.32

[33] On January 5, 1998, LEUG filed a Motion to Strike the Company's Request for Increase in Standby Rates and the testimony and exhibits of Dr. Chamberlin. In an order set forth in U-22137, the Commission transferred to U-22092 certain issues relating to stranded costs. The new rate plan proposed by the Company seeks to restructure its standby rates as a necessary step in its transition to competition. The LPSC Staff and ELI filed an opposition to LEUG's Motion. CII Carbon filed a memorandum in support of LEUG's Motion. The parties presented oral arguments on this issue on February 26, 1998 before the Administrative Law Judge.

[34] Since that time, ELI has filed a request to file the testimony of Bruce Ambrose, adopting the previously filed testimony of John Chamberlin.

versus revenue cap[35] into the second or third FRP proceeding in the same docket, or in the stranded costs proceeding in that docket. In its Memorandum in Support of the Motion to Transfer Testimony, LEUG contended that the rationale for the ALJ's and the Commission's previous decision to not resolve the rate cap issue when no rate increase was at issue no longer existed, since ELI has proposed a standby rate increase. LEUG argued that, under that reasoning, the rate cap issue is therefore ripe at this time and should be addressed in the second FRP proceeding.

In addition to a Motion to Strike the testimony of John Chamberlin, which was denied, LEUG filed a Motion to Transfer Testimony which was granted on March 17th, 1998. The prefiled and hearing testimonies that were transferred addressed the issue of rate cap versus revenue cap and, as

[35] LEUG identified all those pre-filed and hearing testimonies that addressed the issue of rate cap versus revenue cap, and requested that the identified testimony be transferred. The list provided by LEUG is as follows:

Exhibit A: Direct testimony and exhibits of Maurice Brubaker, August 1996,

Exhibit B: Rebuttal testimony of Matthew Kahal, September 1996;

Exhibit C: Rejoinder testimony of Rodney Gilbreath, October 28, 1996;

Exhibit D: Rebuttal testimony of John Chavanne, October 14, 1996;

Exhibit E: Hearing testimony of Maurice Brubaker, November 5, 1996;

Exhibit F: Hearing testimony of Matthew Kahal, November 4, 1996;

Exhibit G: Hearing testimony of Rodeny Gilbreath, November 6, 1996; and

Exhibit H: Hearing testimony of John Chavanne, November 5, 1996.

identifed by LEUG consisted of (1) Direct testimony and exhibits of Maurice Brubaker, August 1996; (2) Rebuttal testimony of Matthew Kahal, September 1996; (3) Rejoinder testimony of Rodney Gilbreath, October 28, 1996; (4) Rebuttal testimony of John Chavanne, October 14, 1996; (5) Hearing testimony of Maurice Brubaker, November 5, 1996; (6) Hearing testimony of Matthew Kahal, November 4, 1996; (5) Hearing testimony of Matthew Kahal, November 4, 1996 [sic]; (6) Hearing testimony of Rodney Gilbreath, November 6, 1996; (7) Hearing testimony of John Chavanne, November 5, 1996. The identified testimony regarding the rate cap issue was transferred to the Stranded Cost Docket by a Ruling on LEUG's Motion dated March 17th, 1998. In order to put the issue before the Commission as to whether there are existing constraints to the implementation of an increased standby rate, the previously submitted testimony regarding rate and/or revenue cap, identified by LEUG was accepted for filing in the Stranded Cost Docket.

Contentions of the Parties

LEUG urged that the FRP Rider filed by ELI should be amended to reflect, consistent with the LPSC's Order No. U-20925, to read as follows: "In no event shall any increase in rates under the FRP Rider and/or relating to Waterford 3 cause any ELI rate schedule to exceed the rates that were in effect on December 31, 1994." LEUG filed a Motion to Transfer the testimony on the rate cap issue from the First FRP Review to the Second FRP Review, the Third FRP Review or the pending Stranded Costs proceedings. The Motion was granted as to transfer of the testimony to the Stranded Costs proceedings. LEUG stated that, "Because this issue will be addressed in the stranded cost proceedings, LEUG provides only a limited analysis of the issue."

LEUG argued that, based on the language in Footnote 1 of the FRP Rider, it might be possible for ELI to raise some

rates above the December 31, 1994 levels as long as the other rates were lower and the overall effect remains revenue neutral. Additionally, the FRP Order permits the pass-through of costs and benefits associated with Waterford 3, which could be in conflict with the cap on rates at the December 1994 levels. LEUG urged that to the extent that the Waterford 3 pass-through would cause rates to increase above the December 1994 levels, such increases should be disallowed.

With respect to the question as to whether the Formula Rate Plan is a revenue cap or a rate cap, Staff did not address the issue and ELI submitted that the issue should only be taken up at such time, if any, that the distinction would have some significance. The matter should be addressed at such time as there might be a violation of a rate cap but not a violation of a revenue cap, or vice versa.

Findings of Fact

56. There was no evidence on the rate cap versus revenue cap issue presented in the current 1997 Formula Rate Plan proceeding.

57. Evidence that was adduced in the 1996 Formula Rate Plan review, and identified as pertaining to the rate cap versus revenue issue, has been removed from the 1996 FRP docket, following ruling on LEUG's Motion to Transfer Testimony, and transferred to the Stranded Costs docket for consideration therein.

Legal Analysis

An administrative agency should make basic findings supported by evidence and ultimate findings which flow rationally from basic findings, articulating rational connection between facts found and orders issued. *Hay v. South Central Bell Telephone Co.*, 475 So.2d. 1052 (La. 1985). All evidence

on the rate cap issue (consisting of testimony) was transferred to the Stranded Costs docket pursuant to a ruling on LEUG's motion issued on March 17, 1998, which ruling was not appealed by any of parties, including the movant, LEUG. Therefore, there is no evidence in this docket on the issue of whether Order No. U-20925 established a rate cap or revenue cap. In the absence of any evidence on this issue, and in view of the ruling on LEUG's motion to transfer testimony, the Commission declines to address that issue in this docket.

Conclusion

There was no evidence on the rate cap issue presented in the current 1997 Formula Rate Plan proceeding. Whatever evidence was adduced in the previous FRP review has been removed from the docket and transferred to the Stranded Costs docket for consideration therein in order to join the issue with the first possible proposed rate increase, i.e., a proposed increase in ELI's Stand-by Tariff. Having no evidence before this Commission on this matter, it is not appropriate to render a decision on the issue.

IT IS THEREFORE ORDERD

1. That the net proceeds of debt shall be used to calculate the capital structure of Entergy Louisiana, Inc.

2. That the continued overpayment by Entergy Louisiana, Inc., of MSS-1 expenses resulting from the inclusion of units in Extended Reserve Shutdown, is imprudent and is to the detriment of Louisiana ratepayers.

3. That all MSS-1 overpayments incurred on or after August 6, 1997 shall be removed from the revenue requirement of Entergy Louisiana, Inc. and credited back to the ratepayers.

4. That having no evidence currently before the Commission on the rate cap / revenue cap issue, the Commission declines to render a decision on the issue at this time.

BY ORDER OF THE COMMISSION
BATON ROUGE, LOUISIANA

December 22, 1998

/s/ Don Owen
DON OWEN, Chairman
DISTRICT V

/s/ Irma Muse Dixon
IRMA MUSE DIXON,
Vice-Chairman
DISTRICT III

/s/ C. Dale Sittig
C. DALE SITTIG, Commissioner
DISTRICT IV

/s/ James M. Field
JAMES M. FIELD, Commissioner
DISTRICT II

/s/ Jack "Jay" A. Blossman Jr.
JACK "JAY" A. BLOSSMAN JR.,
Commissioner
DISTRICT I

APPENDIX D

Entergy Services, Inc. and Gulf States Utilities Company,
Docket No. EL94-13-000

Opinion and Order Affirming Initial Decision
Opinion No. 415

(Issued August 5, 1997)

I. Procedural History

On December 15, 1993, in Opinion No. 385, the Commission authorized: (1) the disposition of Gulf States Utilities Company's (Gulf States) facilities thereby effecting a proposed merger with Entergy Corporation (collectively Entergy); and (2) accepted an amendment to the Entergy System Agreement (System Agreement) that added Gulf States as an operating company subsidiary.[1] Simultaneously, the Commission initiated the current proceeding, under section 206 of the Federal Power Act (FPA),[2] to determine

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[1] *Entergy Services, Inc.* and *Gulf States Utilities Company*, Opinion No. 385, 65 FERC ¶ 61,332 (1993) (Opinion No. 385), *reh'g granted and denied in part*, Opinion No. 385-A, 67 FERC ¶ 61,192 (1994), *appeal held in abeyance*, No. 94-1414 (D.C. Cir. November 17, 1994) (unpublished order). The Entergy Operating Companies are Entergy Arkansas, Inc., Entergy Louisiana, Inc., Entergy Mississippi, Inc., Entergy New Orleans, Inc., and Entergy Gulf States, Inc. When this case was being litigated, the Entergy Operating Companies were named Arkansas Power & Light Company (AP&L), Louisiana Power & Light Company (LP&L), Mississippi Power & Light Company (Mississippi P&L), New Orleans Public Service Inc. (NOPSI), and Gulf States. For purposes of consistency, this Opinion will refer to the company names used during litigation.

[2] 16 U.S.C. § 824e (1994).

whether Entergy had violated the System Agreement by including generating units in extended reserve shutdown (ERS) under the System Agreement's Service Schedule MSS-1 (MSS-1), Reserve Equalization. Specifically, the Commission ordered that:

> a public hearing shall be held in Docket No. EL94-13-000 to consider whether the System Agreement permits the ERS units of the Operating Companies to be included in MSS-1 calculations and, if so, whether such provision is just and reasonable and not unduly discriminatory or preferential.[3]

Because of Entergy's contentions that retroactive refunds were outside the scope of the Docket No. EL94-13-000 proceeding, on April 5, 1994, the Louisiana Public Service Commission (Louisiana Commission), the Mississippi Public Service Commission (Mississippi Commission), and the Mississippi Attorney General (collectively, State Agencies) filed a complaint against Entergy in Docket No. EL94-57-000, seeking retroactive refunds plus interest for Entergy's alleged violation of the System Agreement. The Commission dismissed this complaint, stating that the issue of whether Entergy had violated the System Agreement was already before the judge in Docket No. EL94-13-000, and clarified its discussion in Opinion No. 385, as follows:

> The Commission must first determine whether Entergy did, in fact, violate the System Agreement. If the judge ultimately concludes, based on his review of the record compiled in Docket No. EL94-13-000, that the answer to this question is yes, he should determine the dollar

[3] 65 FERC at p. 62,552.

> amount of such violation for the entire period that the violation occurred. We believe that the judge also should recommend an appropriate remedy.[4]

Following a trial-type evidentiary hearing, an Initial Decision was issued on March 3, 1995.[5] State Agencies, the City of New Orleans (New Orleans), the Arkansas Public Service Commission (Arkansas Commission), Entergy, and Commission trial staff (trial staff) filed Briefs On and Opposing Exceptions to the Initial Decision. Occidental Chemical Corporation (Occidental) filed a Brief On Exceptions to the Initial Decision.

Subsequent to issuance of the Initial Decision, State Agencies filed a motion for oral argument before the Commission. They claim that oral argument is warranted because this case presents a fundamental issue pertaining to when a violation of a formula rate should be remedied. In addition, the Louisiana Commission filed a motion to supplement the record. The Louisiana Commission claims that the record should be reopened to examine additional evidence, namely, Entergy's Electric System 1996 Load & Capability Forecast for 1996-2005, which allegedly shows that ERS units will remain indefinitely in ERS status. The Mississippi Commission filed a response in support of the Louisiana Commission's motion. New Orleans, the Arkansas Commission, and Entergy each filed answers opposing the Louisiana Commission's motion.

[4] *Louisiana Public Service Commission v. Entergy Services, Inc.*, 67 FERC ¶ 61,338 at p. 62,197, *clarified*, 68 FERC ¶ 61,355 (1994).

[5] *Entergy Services, Inc. and Gulf States Utilities Company*, 70 FERC ¶ 63,018 (1995).

II. The System Agreement and the ERS Program

The general purpose of the System Agreement is set forth in Article III of that Agreement, which states:

> The purpose of this Agreement is to provide the contractual basis for the continued planning, construction, and operation of the electric generation, transmission and other facilities of the [Entergy Operating] Companies in such a manner as to achieve economies consistent with the highest practicable reliability of service, subject to financial considerations, reasonable utilization of natural resources and minimization of the effect on the environment. This Agreement also provides a basis for equalizing among the Companies any imbalance of costs associated with the construction, ownership and operation of such facilities as are used for the mutual benefit of all the Companies.[6]

Service Schedule MSS-1, set forth in section 10 of the System Agreement, provides the mechanism for equalizing system reserves among the Entergy Operating Companies. Under Schedule MSS-1, each Operating Company is responsible for a share of the total Entergy system capability; a company's share is equal to the ratio of the company's contribution to the system's twelve-month average peak load. In this way, each Operating Company's reserve ratio is equal to the system reserve ratio. Because in reality some of the Operating Companies provide more than their calculated "share" of the system's capability ("long" companies), while others provide less than their calculated "share" ("short" companies), Schedule MSS-1 provides for "short" companies to make deficiency payments to "long" companies. These

[6] *See* Ex. ENT-2 at p. 12.

payments are based on the amount of capacity that "short" companies are deficient and the average cost of the "long" companies' oil-fired and gas-fired steam units.[7]

The specific language of the System Agreement that has been the focus of review in this proceeding is as follows:

> 10.02 Company Capability
>
> A Company's Capability shall be determined monthly and shall be the sum of available owned or leased generating units, purchases and seasonal or other energy exchange from demonstrated reliable sources as follows:
>
> (a) The total capability of available generating units owned, operated under Operating Agreements for its own benefit, or leased by such Company, which units shall be included at their demonstrated net output measured in megawatts under conditions established by the Operating Committee. A unit is considered available to the extent the capability can be demonstrated and (1) is under the control of the System Operator, or (2) is down for maintenance or nuclear refueling. A unit is considered unavailable if in the judgement of the Operating Committee it is of insufficient value in supplying system loads because of (1) obsolescence, (2) physical condition, (3) reliability, (4) operating cost, (5) start-up time required, or (6) lack of due diligence in effecting repairs or nuclear refueling in the event of a scheduled or unscheduled outage.
>
> The generating units of Gulf States that were in extended reserve shutdown on the date of the merger of Entergy and Gulf States, shall not be considered available for the

[7] *See* 65 FERC at p. 62,495 (explaining terms of the System Agreement).

purpose of determining Gulf States' Capability in the Service Schedule MSS-1 Reserve Equalization calculation until the units are brought into service.[8]

The extended reserve shutdown or ERS program was conceived in the mid-1980s, after the System Agreement was executed. The ERS program was developed and implemented during a time when the Entergy Operating Companies had excess generating capacity and were evaluating methods to reduce costs.[9] The ERS program allowed the Operating Companies to save money by placing generating units in an inactive status and thereby reducing operating staff, maintenance costs, and deferring the costs of repairing units.[10] By deferring maintenance of units and yet preserving units as system reserves, the ERS program also obviated the need to build new capacity. Entergy estimates that, through August 31, 1994, the ERS program produced net savings of more than $65 million for its system.[11]

III. Issues in Dispute

The seminal issue in dispute is whether generating units that Entergy placed in ERS status satisfy the criteria, set forth in section 10.02, quoted above, to be considered "available" for purposes of calculating the Entergy Operating Companies' capability under Schedule MSS-1. The participants filed a Joint Statement of Issues identifying the following for resolution in this proceeding: (1) Did Entergy, in fact, violate the System Agreement?; (2) Assuming a violation of the

[8] Ex. ENT-2 at pp. 32-33. The last paragraph of the quoted language was added as the result of a merger concession offered by the merger applicants and accepted by the Commission in Opinion No. 385. 65 FERC at pp. 62,545, 62,547.

[9] *See* Ex. ENT-17.

[10] *See* Ex. ENT-1 at p. 40.

[11] *See Id.* at pp. 32-33.

System Agreement, what remedy, if any, is appropriate?; (3) Assuming a violation of the System Agreement, what is the dollar amount of such violation for the entire period that the violation occurred?; (4) Should Service Schedule MSS-1 of the System Agreement be amended prospectively to address expressly the ERS issue and if so, how?; and (5) Assuming a violation of the System Agreement, and assuming that refunds are an appropriate remedy, who should be responsible (and in what proportion) for those refunds?[12]

IV. Arguments at Hearing [13]

State Agencies claimed that Entergy knowingly and willfully violated the System Agreement to the detriment of LP&L, Mississippi P&L and their ratepayers. Specifically, State Agencies argued that: (1) Schedule MSS-1 permits equalization of only specified capability and costs, and does not allow the inclusion of capability that is not "available" to meet Entergy system reserve requirements, as defined in Schedule MSS-1; (2) ERS units are not available to serve the needs of the Entergy System, and thus cannot be included as capability under Schedule MSS-1 until they are brought on-line; and (3) Entergy's inclusion of the ERS units in Schedule MSS-1 was illegal conduct that was not justified as an incentive for the Entergy Operating Companies to participate in the ERS program.

As a remedy for this alleged tariff violation, State Agencies contended that Entergy should be required to revise the incorrect billings to the Operating Companies and pay interest on the amounts to be refunded, for the period beginning

[12] The Arkansas Commission disputed the inclusion of Issue (5) in the Joint Statement of Issues to the extent that it may be interpreted to include retail ratemaking matters.

[13] Since, as discussed below, this opinion affirms the Initial Decision's finding that no refunds are appropriate in this proceeding, we do not address Issues (3) and (5) in the Joint Statement of Issues.

January 1, 1987, the date of inception of the ERS program. State Agencies claimed that refunds are required because the tariff violation was patent and inexcusable and would not have been tolerated by an independent purchaser, and Entergy's actions resulted in overpayments to AP&L and NOPSI for a period beyond the normal service lives of the ERS generating units, thus causing added costs to be incurred for reserve purchases.[14] State Agencies also argued that Schedule MSS-1 should not be amended prospectively, as proposed by various parties in an Offer of Settlement.[15]

Trial staff argued that Entergy violated the System Agreement because the contract language does not permit the inclusion of ERS units in Schedule MSS-1. Because the System Agreement is a Commission-approved filed rate, trial staff maintained that the filed rate was not charged. Despite

[14] AP&L and NOPSI placed a proportionately larger share of their capacity in ERS than did Mississippi P&L or LP&L. Entergy Brief on Exceptions at p. 19. The units placed in ERS status had previously been included in Schedule MSS-1. Ex. ENT-20 at p. 13; ENT-1 at pp. 27-28, 40. Continuing to include the ERS units in Schedule MSS-1 resulted in AP&L being more "long" than it would have been, LP&L being more "short," Mississippi P&L being less "long," and NOPSI being less "short." Ex. ENT-20 at p. 14. As a result, State Agencies seek refunds, plus interest, of $19.4 million to LP&L and $16.3 million to Mississippi P&L for the period January 1, 1987 through December 31, 1993. State Agencies seek additional refunds for the post-1993 period. State Agencies Post-Hearing Memorandum at pp. 47-48.

[15] Entergy, the Arkansas Commission, New Orleans and trial staff supported an Offer of Settlement (Ex. ENT-10), included as an appendix to the Initial Decision (70 FERC at p. 65,108), that would address the treatment of ERS units under Schedule MSS-1 in the period subsequent to the Entergy/Gulf States merger. The Schedule MSS-1 provision in the Offer of Settlement would expressly allow the inclusion of the ERS units in the Schedule MSS-1 calculations in certain circumstances and also would clarify what those circumstances would be (*i.e.*, when the Entergy Operating Committee could declare an ERS unit to be available for purposes of Schedule MSS-1).

these violations, trial staff contended that Entergy's practice of including ERS units in the Schedule MSS-1 calculation was reasonable because this approach was consistent with concessions made by the merger applicants, and accepted by the Commission, in its approval of the Entergy/Gulf States merger.[16] Trial staff argued that Entergy should be required to pay refunds not in excess of the time value of the principal of the retroactive refunds (*i.e.*, interest on the difference between Schedule MSS-1 payments with and without the ERS units included in calculations under Schedule MSS-1).[17] Trial staff maintained that this remedy would be consistent with the Commission's refund policy that applies in similar circumstances, *i.e.*, when a utility fails to seek prior approval for recovery of costs through its fuel adjustment clause.[18] Finally, trial staff supported adoption of the revised Schedule MSS-1 language contained in the Offer of Settlement.

Entergy responded that it did not violate the System Agreement by including the ERS units in Schedule MSS-1 because: (1) the Schedule MSS-1 contract language gives the Entergy Operating Committee the discretion to include the ERS units in the reserve equalization calculation; (2) failure to include the ERS units in Schedule MSS-1 would be inconsistent with equalizing the cost of excess capacity on the

[16] In the Entergy/Gulf States merger proceeding, the Commission approved a condition that excluded Gulf States' existing ERS units from Schedule MSS-1 treatment, while allowing the ERS units of the other Entergy Operating Companies to continue to receive Schedule MSS-1 treatment. 65 FERC at pp. 62,545-49. This disparate treatment resulted in Entergy's pre-merger Operating Companies (and their ratepayers) receiving a substantial monetary benefit in the form of a lower equalization responsibility under Schedule MSS-1.

[17] For the period from January 1, 1987—October 14, 1994, trial staff computed the time value as $7,187,195. Ex. S-4 at pp. 14-15; Tr. 846.

[18] *See Western Resources, Inc.*, 65 FERC ¶ 61,271 (1993), *modified*, 66 FERC ¶ 61,120 (1994) (*Western Resources*) (where the Commission first enunciated this refund policy).

Entergy System, which was a major objective of the System Agreement (as recognized and expressly found reasonable by the Commission);[19] and (3) the position advocated by the Louisiana and Mississippi Commissions in the Entergy/Gulf States merger proceeding supports Entergy's interpretation of Schedule MSS-1, and contradicts the position taken by those same commissions in this proceeding.

Entergy also argued that, if a violation of the System Agreement were found, the only appropriate remedy would be to reform the System Agreement prospectively, as proposed in the Offer of Settlement. Entergy claimed that refunds are not appropriate here, even if a tariff violation were found to have occurred, because: (1) it would be inequitable to punish Entergy for taking the initiative to reduce costs and rates by implementing the ERS program; (2) the Louisiana and Mississippi Commission witnesses concede that Entergy acted in good faith and that there is no evidence of improper intent on Entergy's part; (3) there is no evidence of unjust enrichment on the part of the Entergy system as a whole; (4) under the State Agencies' refund proposal, Entergy would under-collect its costs of reserves; (5) core principles of the FPA require that retroactive rate calculations be denied; and (6) judicial precedent supports the Commission exercising its discretion not to order refunds.[20]

Finally, raising arguments similar to those made by Entergy, both the Arkansas Commission and New Orleans contended that Entergy's inclusion of ERS units in Schedule

[19] *Citing, e.g., Middle South Energy, Inc.*, Opinion No. 234-A, 32 FERC ¶ 61,425 at p. 61,952, 61,961 (1985), *aff'd in part sub nom. Mississippi Industries v. FERC*, 808 F.2d 1525 (D.C. Cir.), *vacated in part*, 822 F.2d 1104 (D.C. Cir. 1987), *cert. denied sub nom. Arkansas Public Service Commission v. FERC*, 484 U.S. 985 (1987).

[20] *See, e.g., Towns of Concord, Norwood & Wellesley v. FERC*, 955 F.2d 67 (D.C. Cir. 1992) (*Towns of Concord, et al.*).

MSS-1 did not violate the filed rate, refunds are inappropriate in this proceeding, and Schedule MSS-1 should be amended prospectively as set forth in the Offer of Settlement.

V. The Initial Decision

A. *Did Entergy, in Fact, Violate the System Agreement?*

To determine if a violation of the System Agreement occurred, the judge examined whether the ERS units meet the definition of "available" as provided in Schedule MSS-1. Schedule MSS-1 states that "a unit is considered available to the extent the capability can be demonstrated and (1) is under control of the System Operator, or (2) is down for maintenance or nuclear refueling."[21] The judge found that an ERS unit is neither under the control of the System Operator nor is it down for routine maintenance. In addition, he concluded that, because an Entergy study[22] stated that it would take 8-12 months to bring a typical ERS unit into "available status," the units are effectively in storage and their capability cannot be demonstrated. Thus, the judge found the ERS units are not available for purposes of Schedule MSS-1. Consequently, the judge found that Entergy did, in fact, violate the System Agreement.

B. *Assuming a Violation of the System Agreement, What Remedy, if any, is Appropriate?*

The judge noted that under the FPA the Commission has discretion whether to order refunds.[23] The judge determined that the Commission should exercise its discretion in this proceeding not to order Entergy to pay refunds. The judge based his decision on the following factors: (1) Entergy's actions in creating the ERS program and permitting these units to be included in Schedule MSS-1 equalization

[21] Ex. ENT-2 at pp. 32-33.

[22] *See* Ex. ENT-16.

[23] *Citing Towns of Concord, et al.*

calculations promoted cost savings and efficiency on the Entergy System, and led to substantial savings for ratepayers; (2) the end result was just, reasonable, and not unduly discriminatory; (3) the inclusion of ERS units in the Schedule MSS-1 calculations has existed since the institution of the ERS program in 1987 (without complaint by any of the state regulatory commissions); (4) Entergy's tariff violation was made in good faith, *i.e.*, there is no evidentiary support for State Agencies' claim that Entergy knowingly violated the System Agreement; and (5) the claims of the Louisiana and Mississippi Commissions that they were unaware until this complaint proceeding that Entergy was violating the System Agreement are belied by these parties' arguments in the Entergy/Gulf States merger proceeding.[24]

C. *Should Service Schedule MSS-1 of the System Agreement be Amended Prospectively to Address Expressly the ERS Issue and if so, how?*

The judge noted that this controversy was caused by the fact that the System Agreement was written before the ERS program was instituted and, therefore, the Agreement does not adequately address the treatment of ERS units. The judge found that the proposed amendment to the System Agreement contained in the Offer of Settlement properly sets out the parameters of the Operating Committee's discretion and, notwithstanding arguments to the contrary, is neither ambiguous nor does it provide the Operating Committee with unfettered discretion.[25] Moreover, the judge noted that the Commission's regulations provide a remedy for any abuse of

[24] 70 FERC at p. 65,101; *see* 65 FERC at pp. 62,545-49 (where the Louisiana and Mississippi Commissions' arguments are discussed).

[25] As noted by trial staff: "[T]o prevent the Operating Committee from arbitrarily moving out-of-service units in and out of MSS-1 calculations and thereby manipulating the flow of MSS-1 dollars among the five operating companies, specific guidelines as to what is an MSS-1 includable ERS unit must be in the System Agreement." Ex. S-1 at p. 12.

discretion. Therefore, the judge concluded that Schedule MSS-1 should be amended prospectively, as provided in the Offer of Settlement.

VI. Briefs on and Opposing Exceptions

State Agencies contend that Entergy did not comply with its lawful, filed rate when it included ERS units in Schedule MSS-1 and requests refunds to correct this error. State Agencies argue that the existing language in Schedule MSS-1 permits only available units to be included in Schedule MSS-1, and that ERS units are unavailable; consequently, they should not be included in Schedule MSS-1. State Agencies further argue that the proposed amendment to Schedule MSS-1 should be rejected because: (1) it is unnecessary because the existing contract language is clear and unambiguous; (2) it would improperly grant Entergy broad discretion to include ERS units in Schedule MSS-1 based on subjective criteria; and (3) it would provide inconsistent treatment of an ERS unit (*i.e.*, it can either be available or unavailable depending on certain circumstances). State Agencies also state that Entergy's witnesses testified that ERS units do not satisfy Schedule MSS-1 criteria and that Entergy, by knowingly violating the System Agreement, acted in bad faith. State Agencies urge the Commission not to create a "good faith" rationale for not imposing a refund because no party will ever admit bad faith and utilities will be free to violate their formula rates.[26]

Occidental adopts the exceptions of State Agencies, and also expressly excepts to the judge's failure to remedy Entergy's violation of what Occidental views as a clear and

[26] In addition, State Agencies maintain that Entergy violated the Commission's accounting rules by not placing ERS units in Account No. 105—Plant Held for Future Use. State Agencies Brief On Exceptions at pp. 44-45, 52. We will not address the accounting argument because it is beyond the scope of this proceeding. *See* 67 FERC at p. 62,197.

unambiguous provision. Occidental claims that the judge's failure to impose a remedy is not supported by Commission precedent or policy.

In its Brief On Exceptions, Entergy excepts only to the judge's finding that Entergy violated the System Agreement by including ERS units under Schedule MSS-1. Entergy argues that the judge's interpretation of the System Agreement: (1) was overly narrow, because it focussed on only the definition of unit availability in Schedule MSS-1; and (2) failed to consider all relevant contract terms and the purpose of the System Agreement (*i.e.*, to credit the Operating Companies for capacity that is built to meet expected system needs). Entergy urges the Commission to find that no violation of the System Agreement occurred.

As relevant here, New Orleans excepts to the Initial Decision's finding that trial staff was the only party to address the treatment of ERS units under Schedule MSS-1 during the Entergy/Gulf States merger proceeding. New Orleans argues that the Louisiana and Mississippi Commissions also addressed this issue through their endorsement of the merger condition involving divergent Schedule MSS-1 treatment of Gulf States' ERS units versus those of the pre-merger Operating Companies. Thus, New Orleans contends that these parties should not be rewarded with any refunds because they were aware of, and indeed actively perpetuated, Entergy's practice of including ERS units in Schedule MSS-1 calculations.

Trial staff excepts to: (1) the finding that Entergy was unaware that it was committing a tariff violation; and (2) the ruling that refunds are not an appropriate remedy. Trial staff argues that Entergy should have known that inclusion of ERS units in Schedule MSS-1 violated the terms of the System Agreement because, as the judge found, the plain language of Schedule MSS-1 does not allow such inclusion, and because the record suggests that Entergy knew as early as May 1993

that the ERS units did not meet the requirements for inclusion.[27] Trial staff concludes that the judge should have ordered some level of refunds, not to exceed an amount based on the *Western Resources* method of calculating the time value of the principal of any retroactive refunds.[28]

State Agencies filed a Brief Opposing Exceptions in which it opposes all of Entergy's and New Orleans' exceptions to the Initial Decision, as well as trial staff's argument on exceptions that Entergy should have a limited refund liability. New Orleans, the Arkansas Commission, Entergy, and trial staff filed Briefs Opposing Exceptions.

VII. Discussion

We affirm the judge's findings that Entergy did, in fact, violate the System Agreement, that refunds are not an appropriate remedy in these circumstances, and that the System Agreement should be amended as proposed in the Offer of Settlement.

A. *Entergy Did Violate the System Agreement*

We affirm the judge's determination that the language of the System Agreement permits Entergy to include generating units in Schedule MSS-1 calculations only to the extent that such units are "available."[29] ERS units can only be

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[27] Trial staff Brief On Exceptions at pp. 2-5, *citing* Ex. S-3 at p. 313; Ex. LPSC-12 at p. 313; Ex. S-4 at p. 9; Tr. 524-25.

[28] Trial staff also argues that the Commission could consider lower refund amounts if a proposed remedy based on *Western Resources* is deemed to be too excessive. Trial staff proposes that refunds can be based on the $500 per day limit established in section 316(b) of the FPA, 16 U.S.C. § 825o(b) (1994), or that the time value of money calculation can be based on the period from January 1, 1987, through January 1, 1994, which is the period from inception of the ERS program to the effective date of the Entergy/Gulf States merger. Trial staff Brief On Exceptions at pp. 8-9.

[29] 70 FERC at p. 65,096.

considered eligible for inclusion in Schedule MSS-1 calculations if they meet the System Agreement's qualifications for availability. The System Agreement does not afford the Entergy Operating Committee broad, unfettered discretion to decide which units should be eligible for inclusion in Schedule MSS-1 computations. As noted above, the System Agreement states the following with respect to classifying generating units as "available":

> A unit is considered available to the extent the capability can be demonstrated *and* (1) is under the control of the System Operator, or (2) is down for maintenance or nuclear refueling. A unit is considered unavailable if in the judgment of the Operating Committee it is of insufficient value in supplying system loads because of (1) obsolescence, (2) physical condition, (3) reliability, (4) operating cost, (5) start-up time required, or (6) lack of due-diligence in effecting repairs or nuclear refueling in the event of a scheduled or unscheduled outage.[30]

Thus, as the judge explained, to be considered available, capability must be demonstrated and the units must also be either "under the control of the System Operator" or "down for scheduled routine maintenance." In this case, we affirm the judge's findings that the ERS units do not satisfy these criteria. Entergy acknowledges that many of the ERS units are in need of repair and that the estimated time to reactivate an ERS unit is 8-12 months.[31] Also, as Entergy admitted, the units are not under the control of the System Operator, nor are they down for routine maintenance.[32] Consequently, the ERS units are not available under Schedule MSS-1.

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[30] Ex. ENT-2 at p. 32 (emphasis added).

[31] *See* Ex. ENT-16 at p. 9.

[32] *See* Ex. LPSC-12 at p. 313; 70 FERC at p. 65,096.

B. *Refunds Are Not an Appropriate Remedy*

The ordering of refunds is within the Commission's discretion.[33] Indeed, the Commission's discretion is at its "zenith" when fashioning remedies.[34] In deciding whether to order refunds, the Commission must consider the relevant factors and its decision must be equitable under the circumstances.[35] In this case, the judge found that the Commission should exercise its discretion not to order refunds. We agree with the judge that, based on the relevant factors, the equities in this case support a decision that refunds are not warranted.

The inclusion of ERS units in Schedule MSS-1 calculations did not result in an unjust, unreasonable or unduly discriminatory outcome in the circumstances.[36] The specific equitable factors we rely on in not requiring refunds here, and which also are discussed below, are as follows: (1) there was no unjust enrichment as a result of the violation, given that Entergy as a whole received no net gain from the inclusion of ERS units in Schedule MSS-1;[37] (2) given that there would have been a disincentive to participate in the ERS program without Schedule MSS-1 treatment for the units,[38] Entergy's

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[33] *See, e.g.*, 67 FERC at p. 62,197 n.8.

[34] *Niagara Mohawk Power Corp. v. FERC*, 379 F.2d 153, 159 (D.C. Cir. 1967).

[35] *See Towns of Concord, et al.*, 955 F.2d at p. 76.

[36] *See* Tr. 856; Ex. S-1 at pp. 9-11; Ex. S-4 at p. 5.

[37] As trial staff notes: "In this proceeding, however, the payments in excess of the filed rate did not go to the benefit of the parent company and its shareholders. As I noted earlier, the overpayments were merely part of equalization payments among ratepayers which algebraically added up to zero as far as Entergy as a whole and its shareholders are concerned." Ex. S-4 at p. 9.

[38] *See* Ex. ENT-14 at pp. 15-16, 28-29, 41; Ex. ENT-43 at pp. 132- 33; Ex. S-1 at p. 11; Tr. 656, 918.

actions, both in creating the ERS program and in continuing to include these units in Schedule MSS-1 calculations, resulted in considerable system-wide benefits, in the form of enhanced system efficiencies and cost reductions,[39] that ultimately benefitted ratepayers; (3) the non-Gulf States ERS units were planned and constructed for the benefit of all of the pre-merger Operating Companies, not individual Operating Companies;[40] and (4) nearly every participant in this proceeding, including State Agencies, at one time either believed that the System Agreement permitted the inclusion of ERS units in Schedule MSS-1 calculations, or at least did not protest such treatment.[41]

State Agencies maintain that allowing Entergy to include ERS units in the Schedule MSS-1 computation results in a permanent misallocation of costs.[42] We disagree. By including ERS units in the Schedule MSS-1 computation, Entergy continued the previously-approved equalization approach that was established for excess capacity on the Entergy System.[43] Moreover, if Entergy had not undertaken to reduce costs for its system by implementing the ERS program, these units would have been eligible for inclusion in Schedule MSS-1.[44] We do not believe that the Operating Companies should lose the right to have their costs equalized

[39] *See* Ex. ENT-1 at pp. 39-40, 45-46; Ex. LPSC-8 at pp. 3, 9.

[40] *See* Tr. 102-03; Ex. ENT-1 at pp. 38-41; 70 FERC at pp. 65,101-102.

[41] *See* notes 16, 24 *supra*; Tr. 118-125, 428-30, 433-34.

[42] State Agencies Brief On Exceptions at pp. 55-56.

[43] Tr. 877; *see Middle South Energy, Inc.*, Opinion No. 234, 31 FERC ¶ 61,305 at p. 61,656 (1985); 32 FERC at p. 61,952. The units placed in ERS status had been previously included in Schedule MSS-1.

[44] *See* Tr. 113-14, 951. None of the participants claim that Entergy improperly placed units in ERS status.

when they take advantage of the ERS program, which, we note, provides very significant benefits for the Entergy system.

Additionally, none of the parties to this proceeding objected to Entergy's interpretation, even at the time Entergy's interpretation of Schedule MSS-1 was brought to light during the Entergy/Gulf States merger proceeding. Moreover, as State Agencies recognize, the allocation of excess capacity under Schedule MSS-1 does not allow Entergy as a whole to gain any extra revenue.

We disagree that we are in any way abdicating our regulatory responsibility. This is not a case where we are denying the imposition of refunds because Entergy acted in "good faith."[45] By exercising our discretion not to order refunds, we are simply acting consistent with the equities in this case.[46] Indeed, the record evidence demonstrates that, although Entergy acted in a manner inconsistent with Schedule MSS-1, the end result was just, reasonable, and not unduly discriminatory.

C. *The System Agreement Should be Amended*

Entergy, the Arkansas Commission, New Orleans, and trial staff support the Offer of Settlement, which is designed to address post-merger treatment of ERS units under Schedule MSS-1.[47] The revised language intends to prevent future

[45] It should be recognized, however, as found in *Borough of Ellwood City v. FERC*, 583 F.2d 642, 647-48 (3d Cir. 1978), *cert denied*, 440 U.S. 946 (1979), that good faith may be considered by the Commission in the exercise of its remedial authority.

[46] Insofar as we are exercising our discretion and on this basis are not ordering refunds here, we need not address whether or to what extent section 206(e) of the FPA, 16 U.S.C. § 824e(c) (1994), would bar us from ordering refunds in any event.

[47] *See* Ex. ENT-10.

disputes by allowing ERS units in Schedule MSS-1 calculations pursuant to specific factors. The amendment provides in relevant part as follows:

> A unit is considered available to the extent the capability can be demonstrated and (1) is under the control of the System Operator, or (2) is down for maintenance or nuclear refueling, *or (3) is in extended reserve shutdown (ERS) with the intent of returning the unit to service at a future date in order to meet Entergy System requirements. The Operating Committee's decision to consider an ERS unit to be available to meet future System requirements shall be evidenced in the minutes of the Operating Committee and shall be based on consideration of current and future resource needs, the projected length of time the unit would be in ERS status, the projected cost of maintaining such unit, and the projected cost of returning the unit to service.*[48]

State Agencies claim that the proposed language is ambiguous and does not limit Entergy's judgment to make decisions on ERS units.[49] We disagree. This proceeding arose because of the failure of section 10.02 of the System Agreement to expressly encompass the ERS program. The proposed amendment does so. As the judge stated:

> The proposed amendment to section 10.02 cures the defects. The amendment is neither ambiguous nor does it provide the Operating Committee with unfettered discretion. The amendment sets out the parameters of the Operating Committee's discretion. The regulations of this Commission provide a remedy for any abuse of this discretion.[50]

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[48] *Id.* at pp. 4-5 (emphasis in original).

[49] State Agencies Brief On Exceptions at pp. 60-65.

[50] 70 FERC at p. 65,106.

We thus affirm the judge on this matter.

D. *The Louisiana Commission's Motion to Supplement the Record and State Agencies' Motion For Oral Argument*

We deny the motion of the Louisiana Commission, pursuant to rule 716 of the Commission's Rules of Practice and Procedure,[51] to supplement the record. The note to Line 17 of the document proffered by the Louisiana Commission, the Entergy Electric System 1996 Load & Capability Forecast, reads: "Operational deficits will be made up through short-term purchases, return-to-service units on extended reserve shutdown, or other operational actions." This language demonstrates that, for purposes of the Load & Capability Forecast, the ERS units are not retired, which is consistent with our understanding as well as the reasoning reflected in the Initial Decision. The Load & Capability Forecast, therefore, does not demonstrate a change in circumstances affecting "the very heart of the case" that would warrant reopening of the record.[52] The Initial Decision, and this opinion, are based on a comprehensive record that supports our determinations. Similarly, given the comprehensive record evidence in support of our findings, State Agencies' motion for oral argument is denied.

The Commission orders:

(A) The Initial Decision issued in this proceeding is hereby affirmed, in accordance with the discussion in the body of this opinion.

(B) Schedule MSS-1 is hereby amended, effective as of the beginning of the first complete billing cycle following the date of issuance of this order, to clarify the treatment of ERS units as provided in the Offer of Settlement.

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[51] 18 C.F.R. § 385.716 (1996).

[52] *See CMS Midland, Inc.*, 56 FERC ¶ 61,177 at p. 61,624 (1991).

(C) State Agencies' motion for oral argument is hereby denied.

(D) The Louisiana Commission's motion to reopen the record is hereby denied.

APPENDIX E

Entergy Services, Inc. and Gulf States Utility Company,
Docket No. EL94-13-000

Initial Decision

(Issued March 3, 1995)

Jacob Leventhal, Presiding Administrative Law Judge

Joint Statement of Procedural History

On December 15, 1993, the Federal Energy Regulatory Commission (FERC or Commission) authorized: 1) the merger and reorganization of Entergy Corporation (Entergy) and Gulf States Utilities Company (Gulf States) (collectively hereafter, Entergy Services); and 2) accepted an amendment to the Entergy System Agreement (System Agreement), which added Gulf States as an operating company subsidiary.[1] *Entergy Services, Inc. and Gulf States Utilities Company*, Opinion No. 385, 65 FERC ¶ 61,332 (1993). At the same time, the Commission instituted the present proceeding, under section 206 of the Federal Power Act (FPA), to determine the appropriate treatment of Entergy Operating Company generating units in extended reserve shutdown (ERS) under Service Schedule MSS-1, Reserve Equalization, of the System Agreement. The Commission ordered that:

> a public hearing shall be held in Docket No. EL94-13-000 to consider whether the System Agreement permits the ERS units of the Operating Companies to be

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[1] The other Entergy Operating Companies are Arkansas Power & Light Company ("AP&L"), Louisiana Power & Light Company ("LP&L"), Mississippi Power & Light Company ("MP&L), and New Orleans Public Service Inc. ("NOPSI").

> included in MSS-1 calculations and, if so, whether such provision is just and reasonable and not unduly discriminatory or preferential.

Opinion No. 385, 65 FERC at p. 62,552. Notice of this proceeding appeared in the *Federal Register* on January 7, 1994, thereby establishing March 8, 1994 as the refund effective date. 59 Fed. Reg. 1015 (1994).[2]

All parties to the merger proceeding in Docket Nos. EC92-21-000 and ER92-806-000 were made parties to this Docket No. EL94-13-000.[3] In addition to the Commission Trial Staff (Staff), the following have been active participants:

> Arkansas Public Service Commission (APSC); City of New Orleans (CNO); Entergy Services, Inc. (Entergy); Louisiana Public Service Commission (LPSC); Mississippi Attorney General (MAG); Mississippi Public Service Commission (MPSC); Public Utility Commission of Texas; Sam Rayburn Municipal Power Agency; and Texas Office of Public Utility Counsel.

On February 16, 1994, Entergy Services filed an offer of settlement and, in light of that offer, concurrently moved for suspension of the previously adopted procedural schedule. In a February 25, 1994 Order, the Chief Judge denied the motion to suspend the procedural schedule. *Entergy Services, Inc. and Gulf States Utilities Company*, 66 FERC ¶ 63,009, at p. 65,053 (1994).

Subsequently, in response to an LPSC motion to compel, Entergy Services moved for an order confirming that claims for retroactive refunds were outside the scope of Docket

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[2] In Opinion No. 385, the Commission ordered that the refund date will be 60 days following publication of the Commission's notice in the *Federal Register*. 65 FERC at p. 62,553.

[3] *Blanket Order Granting Interventions*, Docket No. EL94-13-000 (January 12, 1994).

EL94-13-000, as instituted by the Commission. Trial Staff, CNO and APSC supported Entergy Services' position. In an order issued March 31, 1994, the Presiding Judge, responding to this and other motions, suspended the procedural schedule to permit the LPSC and MPSC to file a complaint for retroactive refunds and to seek to consolidate that complaint with this docket.

On April 5, 1994, the LPSC, MAG and the MPSC (collectively Complainants or L/M/MAG) filed a complaint against Entergy Services in Docket No. EL94-57-000. Complainants alleged that by counting ERS units as available capacity, Entergy Services violated the System Agreement. Complainants sought refunds plus interest.

In a June 17, 1994 Order, the Commission dismissed the complaint in EL94-57-000. *Louisiana Public Service Commission, et al. v. Entergy Services, Inc.*, 67 FERC ¶ 61,338 (1994) (June 17 Order). The Commission noted that the issue of whether Entergy has violated the System Agreement was already before the Presiding Judge in Docket No. EL94-13-000 and found no reason to address that same issue in another proceeding. *Id.* at p. 62,197. The Commission clarified its discussion in Opinion No. 385, stating that:

> The Commission must first determine whether Entergy did, in fact, violate the System Agreement. If the judge ultimately concludes, based on his review of the record compiled in Docket No. EL94-13-000, that the answer to this question is yes, he should determine the dollar amount of such violation for the entire period that the violation occurred. We believe the judge also should recommend an appropriate remedy.

Id. The Commission stated that "the decision whether to order refunds in a particular case is committed to the Commission's discretion." *Id.* The Commission also dismissed an LPSC

complaint that Entergy violated the Commission's Uniform System of Accounts by failing to transfer the cost of the ERS units to Account 105 (plant held for future use). *Id.* The Commission reasoned that the complaint was raised at a "procedurally inappropriate time." *Id.*

In a September 22, 1994 Order, responding to an LPSC request for clarification and/or rehearing, the Commission explained that its June 17 Order was not intended as a final resolution of the accounting issue. *Louisiana Public Service Commission, et al. v. Entergy Services, Inc.*, 68 FERC ¶ 61,355 (1994). The Commission also clarified that the dismissal was not intended to prejudge evidentiary issues in Docket No. EL94-13-000. *Id.*

Discovery in this proceeding was conducted over a 10-month period and included numerous data requests and eight discovery depositions. On August 19, 1994, LPSC and MPSC filed prepared direct testimony. Trial Staff previously had filed prepared direct testimony on March 15, 1994. Responsive testimony was filed on September 23, 1994 by APSC, CNO and Entergy Services. On October 14, 1994, prepared rebuttal testimony was filed by APSC, CNO, Entergy Services, LPSC and MPSC. Depositions were taken of each of the nine witnesses presenting testimony.

On October 19, 1994, a joint statement of issues and pre-trial briefs were submitted by the parties in preparation for the hearing. The hearing commenced on October 24, 1994 and concluded on November 1, 1994. There were six days of hearings with 998 pages of transcript and 103 exhibits. Initial Briefs and Reply Briefs were filed by the Louisiana Public Service Commission, Mississippi Public Service Commission and Mississippi Attorney General jointly (L/M/MAG), Arkansas Public Service Commission (APSC), City of New Orleans (CNO), Entergy Services, Inc. (Entergy) and Commission staff (Staff).

Introduction

As noted in the preceding section, the genesis of this proceeding lies in the Entergy Services/Gulf States Utilities (GSU) merger. In that proceeding, Commission staff's witness, Mr. Sammon, questioned Entergy Services' placement of Operating Companies' generation units into ERS under Service Schedule MSS-1 of the System Agreement. Commission staff was the only participant to address this question. The issue was not resolved in the Initial Decision because it was outside the scope of the proceeding. The Initial Decision noted:

> Staff considers the existing practice of treatment of the EOCs' [Entergy Operating Companies] ERS units to be a violation of the System Agreement. Entergy claims the discretionary right to do so under the terms of the System Agreement. This proceeding is not the appropriate forum to adjudicate this alleged violation of the terms of the System Agreement. It is an existing practice, not instituted as a result of the merger. If, in fact there is such a violation, the appropriate action would be the filing of a complaint.

64 FERC ¶ 63,026, at p. 65,114. The Commission affirmed this ruling in Opinion No. 385, which instituted this section 206 proceeding.

Service Schedule MSS-1, in order to equalize costs of generation among the Operating Companies, provides for placement of excess generation units in extended reserve shutdown (ERS). Thus, section 10 of the Agreement, Service Schedule MSS-1, Reserve Equalization, as pertinent here, provides:

> 10.01 *Purpose*
>
> The purpose of this Service Schedule is to provide the basis for equalizing the capability and ownership cost incidental to such capability among the Companies in

such a manner that the capability and reserves of each Company after equalization shall be equal to its Capability Responsibility.

10.02 *Company Capability*

A Company's Capability shall be determined monthly and shall be the sum of available owned or leased generating units, purchases and seasonal or other energy exchange from demonstrated reliable sources as follows:

(a) The total capability of available generating units owned, operated under Operating Agreements for its own benefit, or leased by such Company, which units shall be included at their demonstrated net output measured in megawatts under conditions established by the Operating Committee. A unit is considered available to the extent the capability can be demonstrated and (1) is under the control of the System Operator, or (2) is down for maintenance or nuclear refueling. A unit is considered unavailable if in the judgment of the Operating Committee it is of insufficient value in supplying system loads because of (1) obsolescence, (2) physical condition, (3) reliability, (4) operating cost, (5) start-up time required, or (6) lack of due diligence in effecting repairs or nuclear refueling in the event of a scheduled or unscheduled outage.

The generating units of Gulf States that were in extended reserve shutdown on the date of the merger of Entergy and Gulf States, shall not be considered available for the purpose of determining Gulf States' Capability in the Service Schedule MSS-1 Reserve Equalization calculation until the units are brought into service.

Ex. No. ENT-2 at pp. 32-33.

The participants agreed upon a Joint Statement of Issues, which were tried in this proceeding. This decision addresses those issues *seriatim* below.

Issue I: Did Entergy, in Fact, Violate the System Agreement?

The active participants are divided into three basic groups. LPSC, MPSC, MAG (collectively L/M/MAG) contend that Entergy violated the System Agreement and that refunds should be retroactive as well as prospective. Commission staff (Staff) finds that there was a violation but that the refund obligation should be limited to the time value of the amounts to be refunded. The third view, held by Entergy, Arkansas Public Service Commission (APSC) and the City of New Orleans (CNO), is that there was no violation of the System Agreement. In the event that it is found that there was such a violation, APSC and CNO maintain that retroactive refunds should not be ordered.

L/M/MAG contend that Entergy, in violation of the System Agreement, unilaterally decided to include in ERS, units which were placed in long term storage and which were not available as reserves. Citing specific examples, L/M/MAG say that many of these units were in a dilapidated condition requiring extensive repair and could not be used to serve system loads. According to L/M/MAG, the evidence shows that these ERS units could not be relied upon for reserves, could not be listed as reserves on reliability reports, could not be sold as reserves and Entergy would not purchase similar units to meet its own reserve requirements.

L/M/MAG contend that Entergy included these units in ERS for its own purposes—to stabilize cash-flow. L/M/MAG believe that Entergy wanted to be able to forecast variations in cost resulting from the System Agreement and thus be able to avoid the necessity of going to retail regulators for rate increases.

L/M/MAG argue that MSS-1 requires a unit to be available before it can count as capability. It provides that a unit is

available when its capability can be demonstrated and (1) is under the control of the System Operator, or (2) is down for maintenance or nuclear refueling. These parties claim that the System Agreement does not provide discretion to the Operating Committee to determine that the conditions are met to make a unit available; but it does provide discretion to declare units unavailable. The System Agreement provides discretion to determine that units are not available if they are of "insufficient value in supplying system loads." This insufficient value may result from obsolescence, physical condition, reliability, operating cost, start up time required, or lack of due diligence in effecting repairs or nuclear refueling in the event of an outage. L/M/MAG contend that the ERS units cannot possibly be termed "available" and therefore, Entergy violated the System Agreement.

Staff agrees that Entergy violated the System Agreement from the inception of the ERS program, January 1, 1987 through the end of the pre-merger period, December 31, 1993, by including ERS units in MSS-1 computations despite the language of the System Agreement. Staff claims, as did L/M/MAG, that ERS units were included in MSS-1 calculations when they were neither under the control of the System Operator and available for dispatch nor down for maintenance or nuclear refueling.

Staff cites *Arkansas Louisiana Gas Co. v. Hall*, 453 U.S. 571, 578 (1981), for the proposition that the filed rate doctrine forbids a regulated entity to "charge rates for its services other than those properly filed with the appropriate federal regulatory authority." Staff argues that the System Agreement is a filed rate and the only rate that is legal.[4] Staff

4 Staff cites additional cases discussing the filed rate doctrine such as *Montana-Dakota Utilities Company v. Northwestern Public Service Co.*, 341 U.S. 246, 251-52 (1951) and *Nantahala Power & Light Co. v. Thornburg*, 476 U.S. 953, 962-67 (1986).

notes that Entergy acknowledges the proposition that the System Agreement is the filed rate. As such, it is the only legal rate.

Staff disputes an Entergy claim that the System Agreement confers broad latitude on the Operating Committee to carry out the efficient and effective management of the System Agreement. As a result, Staff finds that $19,420,499 was shifted from the ratepayers in Louisiana and Mississippi to ratepayers in Arkansas and New Orleans in violation of the filed rate doctrine.

Staff contends that Entergy's interpretation of the System Agreement is inconsistent with its wording. According to Staff, at the merger hearing, Entergy witness Gallaher testified that when the Operating Committee placed units into ERS it expected to recall them within five years. Entergy's purpose of not removing operating ERS capacity from MSS-1 was to stabilize cash-flows and expectations relating to MSS-1 transactions. *See* Ex. No. S-2 at p. 150. Staff's witness considers this to be valid.

Although Staff witness Sammon testified that the current MSS-1 treatment of ERS violates the System Agreement and the filed rate doctrine, he found Entergy's practice to be reasonable. Staff notes that the Commission approved the Entergy/GSU merger based on the expectation that the pre-existing Entergy Operating Companies would receive credit for their ERS units while GSU would not. Denying credit to these companies would reduce the cushion of merger benefits upon which the Commission relied in finding that no Operating Company would be harmed by the merger.

Staff claims that the availability provisions of Article 10 of the System Agreement were designed to provide an incentive to the Operating Companies to keep their generating units in good repair and "on line" except for maintenance and refueling. If a company failed to keep a generating unit in

good repair such that the unit was forced out of service, that Operating Company would suffer a detriment under MSS-1 by having its level reduced. Staff considers this incentive/detriment effect under MSS-1 to be inappropriate for units in ERS status. Entergy witness Gallaher cited the six criteria (enumerated by L/M/MAG above) for judging whether a unit is considered unavailable and concluded that ERS units were more available than unavailable. Staff disagrees with this analysis. Staff finds that Entergy does not have unlimited discretion to declare a unit available that does not meet the initial definition of available in section 0.02(a). Staff believes that the ERS units do not meet these criteria.

Entergy, CNO, and APSC argue that Entergy did not violate the System Agreement. They contend that the Operating Committee's inclusion of ERS units in MSS-1 calculations was consistent with the System Agreement.

Entergy claims that Schedule MSS-1 was instituted to apportion among its Operating Companies the cost responsibility for the considerable amount of excess generation capacity that was expected to exist on the Entergy System. The existence of MSS-1 has enabled Entergy to avoid the cost of constructing new generating facilities and the ERS units are now being returned to full service. Entergy notes that LPSC and MPSC participated fully in the recent Entergy/GSU merger proceedings without perceiving any rate violation on Entergy's part. Entergy comments that it acted in the good faith belief that its ratemaking approach was consistent with the System Agreement and that its actions reduced costs for all Operating Companies.

Entergy urges that the System Agreement be interpreted in a way that is consistent with its purpose. Section 4.01 of the System Agreement expressly provides for the sharing of excess capacity. This purpose is implemented by Schedule MSS-1. Entergy states that at the time that the Commission approved the System Agreement and the allocation of the

Grand Gulf plant among the companies, it recognized that such excess capacity existed and specifically approved the Agreement's intent to equalize the cost of such excess capacity. Entergy I.B. at p. 10 (citing *Middle South Energy, Inc.*, 31 FERC ¶ 61,305, at pp. 61,655-56 (1985); *Middle South Services, Inc.*, 32 FERC ¶ 61,425, at p. 61,952 (1985)).

Entergy notes that the courts have observed that "[a]mbiguity easily arises when the contract is applied to its subject matter in changed circumstances," and in such circumstances the contract "should be interpreted in light of the changed circumstances to accomplish what the parties intended." *See Pennzoil Co. v. FERC*, 645 F.2d 360, 388 (5th Cir. 1981) (citing *Richmond Power & Light v. FPC*, 481 F.2d 490, 499 (D.C. Cir.), *cert. denied*, 414 U.S. 1068 (1973)).

Entergy says that no one contests the fact that it made economic sense for the System as a whole to place the units in ERS status. If there had been no excess capacity, the units would have been repaired promptly. Since excess capacity existed, repair of the units placed in ERS would have been wasteful.

Entergy contrasts the testimony of LPSC witnesses regarding "available" here and in two other cases, where they testified that units in "extended cold shutdown" status should be counted as available to meet load requirements. Entergy urges that the System Agreement be interpreted to give effect to all of its terms. Thus to accept the interpretation advocated by L/M/MAG would defeat the parties' intent to equalize excess capability.

Entergy points out that in the recent merger proceeding, LPSC witness Baron (and others) proposed amending the MSS-1 to exclude Gulf States' ERS units from receiving equalization. Entergy notes that the witness conceded under cross-examination that his current interpretation would render his amendment unnecessary.

Entergy says that its interpretation conforms to the intent of the System Agreement. The ERS program was conceived after the System Agreement was drafted. The Operating Committee was aware that the excess capacity on the System was not caused by the ERS units or by the Operating Companies, but was caused by all the generating units on the System. Thus, it says, it would be unfair to single out the Operating Companies that put units in ERS and impose a detriment on them by denying equalization.

Entergy acknowledges that several attributes of the ERS units do not permit a ready fit under section 10.02(a) of MSS-1's description of available or unavailable. Therefore, the Operating Committee unavoidably exercised some judgment and discretion. For example, section 10.02 says that units are "available" if "down for maintenance." Entergy argues that though ERS units are not down for routine maintenance, they are down for deferred maintenance. Although these units are not under the unilateral control of the System Operator, an ERS unit, on request, may be readied to meet unexpected system needs. Furthermore, under section 10.02, a unit is considered unavailable only, if "in the judgment of the Operating Committee it is of insufficient value in supplying system loads" based upon six factors. In the opinion of the Operating Committee, none of these factors would require classifying these units as unavailable.

CNO espouses many of the arguments advanced by Entergy. It notes that the ERS units were built for the System as a whole. It believes that all the Operating Companies caused the costs of the ERS units to be incurred. Therefore, CNO argues that principles of fairness in ratemaking require that all of the Operating Companies contribute to these costs. Entergy, Staff, APSC and CNO support an amendment to the System Agreement to clarify that Entergy can properly include units in ERS in MSS-1.

CNO counters the argument made by L/M/MAG that accepting their proposal would put each Operating Company in the same position they would have been if Entergy had not violated its tariff. CNO contends that each Operating Company would not have made the same recommendation to place units in ERS if it could not count ERS units in MSS-1 calculations. Specifically, it would have been imprudent for New Orleans Public Service, Inc. (NOPSI) to do so.

Along with Entergy, CNO finds that the language of the System Agreement is not clear regarding how treat [sic] ERS units. CNO points out that the issue of whether or not Entergy could count ERS units in MSS-1 calculations under its existing tariff language was expressly raised by Staff witness Sammon early on in the merger proceeding. Despite this fact, CNO says that the LPSC was a leading advocate of the mitigating condition adopted by the Judge and the Commission, whereby the ERS units of the preexisting EOCs continued to be included in MSS-1 calculations but the ERS units of GSU were excluded until actually returned to service. CNO shows that MPSC witness testified that MPSC previously supported the continued inclusion of ERS units in MSS-1 because at the time, he believed it to be in the best interests of its ratepayers to include them. MPSC only decided to protest Entergy's inclusion of the ERS units of Arkansas Power & Light Co. (AP&L), Louisiana Power & Light Co. (LP&L), Mississippi Power & Light Co. (MP&L) and NOPSI after it realized that it might be able to obtain some monetary refunds.

CNO contends that it is particularly unfair to a short company, such as NOPSI, to deny MSS-1 treatment of its ERS units. As the smallest company on the system, NOPSI would be hard hit by exclusion of its 256 mw capacity in ERS. Because it is a short company, which makes MSS-1 payments to the long companies on the System, the MSS-1 formula does not provide for the recovery of depreciation

costs, operation and maintenance expenses, insurance and taxes incurred by NOPSI. If the inclusion of NOPSI's megawatts of ERS capacity is disallowed, CNO says, NOPSI will bear the costs of its own ERS units while also paying increased MSS-1 payments to the long companies.

CNO agrees with Entergy that the ERS units are available for planning reserve purposes and provide benefits to the System. CNO argues that the real issue in this proceeding is not whether ERS units are in fact technically available for dispatch but whether such capacity should be used in calculating MSS-1 charges among Operating Companies. CNO believes considerations of equity dictate that they should.

CNO cites other instances where units that are not available for instant dispatch are included in MSS-1 calculations under the System Agreement. CNO contends that the ERS units provide not only future benefits but current ones as well. Many of the ERS generating units have been returned to service. Other costs for maintenance as well as for new construction have been deferred.

CNO interprets the MSS-1 program as a cost-sharing mechanism under which capacity is equalized among the long and short companies by comparing the percentage share of total System capacity which each company owns or has available to it under contract, with its percentage share of System demand.

In rebuttal, L/M/MAG assert that Entergy and others, ignoring relevant language of the System Agreement, rely upon a strained contention that the agreement is unclear. They maintain that the "equity considerations" raised by Entergy and its supporters require that the ratepayers of LP&L and MP&L bear the costs of an illegal cost allocation rather than Entergy's shareholders.

L/M/MAG say that Entergy violated the plain language of the tariff and allocated the cost of ERS capacity to customers in the wrong jurisdiction.

L/M/MAG dispute the claim that the System Agreement intended to equalize excess capacity. They cite section 4.01 of the System Agreement:

> Any Capability in excess of the Capability Responsibility of a Company that may exist in the system of one or more Companies as a result of installation of facilities in accordance with the provisions of the generation addition plan shall be equalized among the Companies in accordance with the provisions of the applicable Service Schedule.

Ex. No. ENT-2 ¶4.01, at 16. L/M/MAG find that the agreement does not provide for equalizing excess capacity *per se*, but equalizes that in excess of a Company's Capacity Responsibility. L/M/MAG state that the cited provision refers to capability and a generating unit does not qualify as capable under the System Agreement unless an output in megawatts can be produced by the unit.

L/M/MAG refer to Entergy witnesses' testimony that only reserve capacity is to be equalized. L/M/MAG claim that reserves are units that can be called on to serve load. Since the ERS units cannot serve load, L/M/MAG believe they do not qualify under Schedule MSS-1. L/M/MAG cite *Middle South Energy, Inc.*, 31 FERC ¶61,305, at p. 61,635 (1985), "[T]he older units now have operating characteristics directly related to use as reserve capability, and it is only reserve capacity that is to be equalized under the System Agreement." Again, L/M/MAG point out Commission language in *Middle South Energy, Inc.*, 32 FERC ¶61,425, at p. 61,959 (1985), "[T]he intent of the System Agreement has not been to specifically equalize costs, but rather to equalize any imbalance of costs associated with facilities used for the mutual benefit of all the companies."

L/M/MAG explain that in the merger proceeding, they did not focus on whether the placement of ERS units in MSS-1 constituted a possible tariff violation. At that time, their analysis concentrated on the impact of GSU's entry into the System. They say they accepted without scrutiny the representation of Entergy that it had the discretion to count ERS units under MSS-1. In any event, L/M/MAG argue that there is no ambiguity in the definition of available in the System Agreement and no discretion for the Operating Committee to declare ERS units available.

Entergy, in its Reply Brief, again argues that an LPSC sponsored witness in another FERC case, advised the Commission that because ERS units can be returned to service when needed they must be included in an Operating Company's capability for reserve purposes. *See* Ex. No. CNO-13 at p. 17.

In reply to L/M/MAG, Entergy says that section 3.01 of the System Agreement contemplates equalization of facilities that provide "mutual benefit" for the Companies. Entergy insists that MSS-1 is not confined to certain kinds of units or only to units that are actually being dispatched. Rather, it applies to all generating capability to quantify the reserves that are equalized.

Entergy maintains that the only way to interpret the Agreement is to apply it in a way that effectuates its purpose and gives it meaning as a whole. Entergy insists that the Operating Committee determination to continue to include ERS units in MSS-1 permitted efficient operation of the System.

Ruling

The issue under consideration here is whether Entergy has violated the System Agreement in placing certain ERS units into Schedule MSS-1. Many of the arguments regarding this issue in the post hearing briefs also address what adjustments

should be ordered in the event that a violation has been committed. Such arguments will be dealt with later on in the decision.

L/M/MAG characterize Entergy's treatment of ERS units as a "blatant" violation of the terms of the System Agreement. *See* L/M/MAG I.B., at p. 1. An interpretation, which has been in existence and followed by all of the parties since its inception in 1987, can hardly be characterized as blatant. As a matter of fact, it was a Staff witness in the merger proceeding that raised this issue for the first time. Furthermore, in the merger proceeding, LPSC and MPSC supported the exclusion of GSU's ERS units from MSS-1 and the adoption of an amendment to the System Agreement to accomplish this result. Under these circumstances, I cannot find this characterization valid.

Entergy can only place ERS units into MSS-1 in conformance with the System Agreement. Section 10.02(a) provides that "a unit is considered available to the extent that the capability can be demonstrated and (1) is under control of the System Operator, or (2) is down for maintenance or nuclear refueling." Entergy does not have untrammeled discretion to declare ERS units available for placement in MSS-1.

Thus in order for Entergy to consider ERS units "available," capability first must be demonstrated. Then, Entergy must show that the units are under the control of the System Operator or that the units are down for maintenance or nuclear refueling.

As Entergy admits, many of the ERS units are in a state of ill repair and would require refurbishing before they could be made serviceable. In 1987, Entergy performed an Extended Reserve Shutdown Study which identified that, "The time to reactivate the plants or units to an available status is estimated to be 8-12 months unless otherwise specified." *See* Ex. No.

ENT-16 at p. 9. As these units are in storage, capability cannot be demonstrated. Furthermore, an ERS unit is neither under the unilateral control of the System Operator nor is down for routine maintenance or nuclear refueling.

Entergy argues that one should look at the section in its entirety. Thus one must not only look to the tests for availability but also at the six elements for unavailability set forth in section 10.02(a). Entergy believes that the ERS units do not meet the standard for available or unavailable, but concludes that they are more like available units than unavailable units.

It is true that the Agreement must be read in its entirety. Entergy's argument that the ERS units are more available than unavailable is not helpful in determining eligibility for MSS-1. The test is whether the units meet the definition of available. I find that the ERS units are not available within the definition of availability. The language in the Schedule in this regard is clear and unambiguous.

The fact that the ERS program leads to System efficiencies and reduced costs for all Entergy Operating Companies is laudable. However, the ERS units must meet the clear terms of the Schedule in order to be included in MSS-1.

It is acknowledged that Entergy's actions in this regard were made in good faith. Good faith, however, cannot excuse a violation.

There is no dispute that the System Agreement is the filed and legal rate. Tr. 505.[5] The filed rate is the only legal rate. It has been long established that a regulated utility may not charge rates for its services other than those properly filed

[5] Q. (by Mr. Fontham) Now would you agree that the System Agreement is the filed rate?
A. (by Mr. Gallaher) Yes.
Q. And it is the legal rate?
A. Yes.

with the appropriate federal regulatory authority. *Arkansas Louisiana Gas Co. v. Hall*, 453 U.S. 571, 576-79 (1981).

Entergy acknowledges that the ERS program was not contemplated at the time the System Agreement was drafted and no provision expressly addresses it. Ex. Nos. ENT-1 at p. 28; ENT-14 at p. 27. Entergy relies on its interpretation that the System Agreement conferred discretion upon the Operating Committee to include ERS units in MSS-1. The plain language of section 10.02(a) is not susceptible to such an interpretation. The ERS units are not available and therefore cannot be included in MSS-1 calculations.

I find that Entergy did, in fact, violate the System Agreement.

Issue II. Assuming a Violation of the System Agreement, What Remedy, if any, is Appropriate?

L/M/MAG argue that Entergy's tariff violation resulted in overpayments by LP&L and loss of receipts by MP&L that should never have occurred. L/M/MAG believe the appropriate remedy requires Entergy to correct the tariff violation by revising the incorrect bills and paying interest on amounts to be refunded. L/M/MAG claim that this remedy is consistent with the Federal Power Act, the filed rate doctrine, and the decisions approving the System Agreement as a formula rate. L/M/MAG I.B. at pp. 28-42.

L/M/MAG claim that under the Federal Power Act, the FERC is obliged to ensure that rates charged to customers are just, reasonable and nondiscriminatory. *See* 16 U.S.C. § 824d(a). L/M/MAG state that the rates filed with the FERC become the filed, legal rates, and utilities must comply with their terms. According to L/M/MAG, the FERC generally orders refunds when it finds that a utility violated a filed rate. Here, they maintain that the only way to ensure that the filed rate is followed is to revise the bills in accordance with the formula in the System Agreement.

L/M/MAG dispute Entergy's justification for including ERS units in capability under MSS-1 as necessary to avoid a disincentive for the Operating Companies to participate in the ERS program. They argue that Entergy's tariff violation permitted the companies with proportionately greater ERS capacity (long companies) to obtain far more equalization credits than if the units had remained in service for their projected lives.

L/M/MAG find that the only disincentive for a unit placed in ERS and then returned to active status is a delay in the receipt of a credit. If the tariff were followed, the company would forego MSS-1 credit while the unit was in ERS but would receive credit for the remaining service life of the unit after it was returned to service. Thus, Ex. No. LPSC-24, used on cross examination of Staff witness Sammon, hypothetically compares 10 mw units that are kept in service (option 1) for a period of eight years against being placed in ERS for the same period (option 2). Under option 1, an annual credit of $60,000 is received in each of the first three years; under option 2, the credit is received in each of the last three years. In each case the units receive the same credit totalling $180,000.

L/M/MAG claim that Entergy's practice of placing ERS units in MSS-1 allows the long companies to receive credits or payments in excess of what they would receive if the units were included in MSS-1 for their service lives. This is illustrated by Ex. No. LPSC-25, a hypothetical which uses the same assumptions as Ex. No. LPSC-24. The exhibit demonstrates that allowing the unit to count while in ERS as well as after it comes back in service, would permit an Operating Company, such as NOPSI, to receive an annual credit of $60,000 for each of eight years, totalling $480,000. L/M/MAG believe this exhibit shows that Entergy's tariff violation permits the owning company to receive payments

for the full service life of the unit, plus the time it is in ERS. Thus refunds are needed to cure such a tariff violation. *Id.* at pp. 21-23.

On the other hand, Entergy, APSC and CNO argue that retroactive refunds are inappropriate in this proceeding. Staff recommends that Entergy refund the time value of the refunds that would otherwise be due. All four propose that the appropriate remedy is to reform the System Agreement prospectively.

Staff believes that refunds not in excess of the time value of the principal of the retroactive refunds are an appropriate remedy. Staff bases its opinion on the Commission's policy stated in *Western Resources, Inc.*, 65 FERC ¶ 61,271 (1993).

The Commission enunciated a new policy in *Western Resources*. In applying the policy, the Commission examines whether it has allowed, rejected, or not ruled on fuel adjustment clause recovery for the cost in question. It also examines whether customers enjoyed savings or suffered losses from the utility's unilateral action. 65 FERC at p. 62,252.

In this case, Staff asserts that Entergy has met the requirements in order to be eligible to be allowed to refund only the time value of the principal, rather than both the principal and its time value. First, Staff claims that Entergy could have obtained approval to include ERS units in MSS-1 calculations. Staff argues that Entergy would have met the ongoing benefits test since witnesses on both sides of the issue agreed that the ERS program has benefitted the System. Staff also claims that the Commission would have approved including ERS units in MSS-1 calculations if given the opportunity as demonstrated by its inclusion of the ERS units in MSS-1 calculations as part of the conditions for the merger proceeding.

The amount of the principal is $19,420,499 for the period January 1, 1987 through December 31, 1993. *See* Ex. No.

ENT-20 at pp. 5-6, 13-18. This value is the difference in MSS-1 payments that result from excluding ERS units, as calculated by Entergy witness Reagan. When computed from January 1, 1987 through October 14, 1994, the date Staff witness Sammon filed his Prepared Rebuttal Testimony, the time value of this amount is $7,187,195. Staff I.B. at p. 22.

L/M/MAG believe that *Western Resources* doesn't apply here because Entergy embarked on the ERS program primarily to benefit shareholders and violated the tariff to stabilize cash-flows among the companies and avoid rate examinations. According to L/M/MAG, in *Western Resources* the company incurred a $500,000 expense to produce a $1 million fuel clause saving to ratepayers. L/M/MAG assert that stockholders could not benefit from the buy-down cost in *Western Resources* because all the savings were captured by the fuel clause. In this case, L/M/MAG claim that virtually all of the savings from the ERS program benefitted stockholders. L/M/MAG state that this action misallocated costs among customers and required LP&L and MP&L to incur higher costs than they would have incurred if the tariff were followed. Thus L/M/MAG claim that full refunds are required. L/M/MAG I.B. at pp. 34-38.

Staff challenges L/M/MAG's assertion that all of the savings from the ERS program have benefitted stockholders, whereas in *Western Resources* the utilities incurred costs which benefitted ratepayers. Staff states that there is no dispute that the ERS program produced substantial savings; the dispute is what portion went to ratepayers and what portion to shareholders. Staff claims that the mere fact that there were no explicit reductions in the filed rates does not mean that the ERS savings did not benefit ratepayers. Rather, the ERS savings may have offset increases in costs and avoided the need for the Operating Companies to seek rate increases. *See* Ex. No. S-4 at p. 13.

Entergy contests Staff's proposal of a monetary sanction totaling $7.19 million based on the Commission's decision in *Western Resources*. Entergy believes that this remedy is unreasonable and unlawful. Entergy emphasizes three points: (1) the logic underlying the remedy in the *Western Resources* doctrine does not apply to the facts in this case; (2) a $7.19 million fine is completely out of proportion to what Entergy allegedly did wrong and is 70 times higher than any refund ever required under the *Western Resources* doctrine; and (3) the Staff's $7.19 million remedy is 500 percent higher than the maximum amount of monetary sanction allowed under the Commission's civil penalty jurisdiction. Entergy states that even Staff witness, Mr. Sammon, testified in his rebuttal testimony and at the hearing that the refund he calculated under this approach is "harsh" and "excessive" "in comparison with what Entergy did wrong." *See* Ex. No. S-4 at pp. 15-16; Tr. 875. In this case, Entergy claims that the Operating Committee adopted a good faith interpretation of an ambiguous contract, a situation quite unlike *Western Resources*. Entergy I.B. at pp. 46-53.

Entergy argues that the only appropriate remedy required is to reform the System Agreement prospectively. Entergy contends that no refunds or monetary penalties are appropriate in this case.

Entergy states that the Federal Power Act does not require refunds when a filed rate is violated. *Id.* at p. 27 (citing *Towns of Concord v. FERC*, 955 F.2d 67, 75-76 (D.C. Cir. 1992)). Entergy asserts that the controlling standard is whether refunds are required as a matter of equity—whether it would shock the conscience if a refund were not required. *Id.* (citing *Towns of Concord*, 955 F.2d at pp. 75-76). Entergy believes that the Commission should assess their conduct in light of the equitable factors recognized by the Commission and the courts. These equitable factors include whether the violation was deliberate; whether failure to award refunds will result in

an unjust enrichment; whether refunds would result in the likelihood of a utility under-collecting its costs; and whether the result in the case is consistent with the goals of the Federal Power Act.

Entergy claims that it implemented a program that made everybody better off than the status quo; operated its system efficiently; accomplished these beneficial results in a manner that preserved the cost equalization recently approved by the Commission; and the Commission would have, in Staff witness' judgment, approved this again a few months later in 1986, if asked. Entergy contends that the witnesses for the LPSC and MPSC admitted there is no evidence that Entergy acted in anything other than good faith. Entergy asserts that LPSC and MPSC have provided no evidence of unjust enrichment. Entergy further argues that the ERS program is consistent with the core principles of the Federal Power Act: efficiency, reliability, coordination, just and reasonable and nondiscriminatory rates, and recovery of legitimate costs. Entergy believes the L/M/MAG request for retroactive rate recalculations violates the core principles of the FPA.

Furthermore, Entergy states that the L/M/MAG claims are predicated on the notion that the right remedy is a retroactive recalculation of the Operating Companies' MSS-1 rates over the last seven years. According to Entergy, the law establishes that such retroactive rate calculations are particularly inappropriate and inequitable in either of two types of cases: (1) where the utility's conduct in question created net benefits for ratepayers, and (2) where the issue involves allocation of costs within a holding company system. *Id.* at pp. 28-29 (citing *Minnesota Power & Light Co. v. FERC*, 852 F.2d 1070 (8th Cir. 1988); *Central Illinois Public Service Co., v. FERC*, 941 F.2d 622 (7th Cir. 1991); *Gulf Power Co. v. FERC*, 983 F.2d 1095 (D.C. Cir. 1993)). Entergy insists the ERS program saved costs for wholesale customers and lowered MSS-1 rates. This case also involves a cost allocation formula, Service Schedule MSS-1. Thus Entergy believes retroactive rate recalculations are inappropriate in this proceeding.

Entergy challenges L/M/MAG's argument that Entergy "knowingly violated the tariff in a way that never would have been countenanced by an independent party." Entergy R.B. at p. 32. According to Entergy, the evidence shows that when the Operating Committee decided to continue to include ERS units in the MSS-1 calculations, it was acting in the good faith belief that it was applying the tariff as filed.

L/M/MAG challenge Entergy's argument that the refund standard to be applied is "whether it would shock the conscience if a refund were not required." L/M/MAG assert that the case cited by Entergy, *Towns of Concord v. FERC*, does not contain the term "shock the conscience" or "shocking the conscience." L/M/MAG claim that the case simply holds that the Federal Power Act does not require the FERC to grant refunds for violations of filed rates under all circumstances. According to the decision, "Customer refunds are a form of equitable relief, akin to restitution, and the general rule is that agencies should order restitution only when 'money was obtained in such circumstances that the possessor will give offense to equity and good conscience if permitted to retain it.'" 955 F.2d at pp. 75-76.

L/M/MAG insist that the equitable standard set out in *Towns of Concord* is more than satisfied. They claim that there is no equitable basis to require ratepayers in Louisiana and Mississippi to bear costs that never should have been assigned to them in the first place. L/M/MAG state that Entergy violated clear language requiring that units be "available" before they could be counted as MSS-1 capacity. Furthermore, L/M/MAG claim that Entergy's position is inequitable because its action causes ratepayers to pay twice for the same capacity. Entergy's interpretation requires

ratepayers to support the units under MSS-1 while they are in storage as well as when they are available.

In its Reply Brief, Entergy argues, as does CNO, that L/M/MAG's charts (Ex. Nos. LPSC-24 and LPSC-25) are based on incorrect assumptions. With respect to LPSC-25, Entergy explains that L/M/MAG rely on the assumption that a generating unit can be operated for precisely the number of years of its depreciation life: no more, no less. Entergy claims, however, that generating units often are operated beyond the time period adopted for depreciation purposes. Their second assumption is that after a unit is fully depreciated it has a cost identical to what it was before it was fully depreciated. Entergy claims that the exhibits should have reflected that MSS-1 charges would go down because costs are reduced due to depreciation.

CNO believes that the appropriate and equitable remedy is to amend the System Agreement prospectively to clarify that the ERS units of AP&L, LP&L, MP&L and NOPSI will be included in MSS-1 calculations. CNO argues that the L/M/MAG request for retroactive refunds should be denied. CNO claims that the practical effect of these refunds would be to impose unjust and unreasonable rates on AP&L and NOPSI. *See* Ex. No. S-4 at p. 5.

CNO asserts that L/M/MAG's request for this large amount of refunds is based on the assumption that history would have repeated itself in the exact same manner if Entergy had instead decided, back in late 1985 and early 1986, that the language of its tariff precluded it from continuing to count ERS units. CNO states that LPSC and MPSC have not proven that each of the individual Operating Companies and their ratepayers will be placed in the same position they would have been simply by recalculating the System bills. CNO claims that if Entergy had instead decided not to count the ERS units in MSS-1, the decision-making of the individual

companies, as well as savings and costs to these companies and their ratepayers, may have been quite different.

CNO argues that it is unrealistic and counter-intuitive to believe that NOPSI's decision-making would have remained the same if its ERS units had not been counted in MSS-1 calculations. Any savings which were expected to be achieved by NOPSI from the placement of its units in ERS would be wiped out entirely by the removal of those units from MSS-1 calculations. *See* Ex. No. CNO-1 at pp. 23-27.

CNO also challenges L/M/MAG's hypotheticals, which attempt to demonstrate that the only consequence to an EOC from excluding an ERS unit that it owns from MSS-1 calculations while it is in ERS status is a delay in the receipt of credit under MSS-1 for that particular unit until the time when it is returned to service. L/M/MAG argue that Ex. Nos. LPSC-24 and LPSC-25 show that an owning company receives $300,000 more of MSS-1 credit by including its hypothetical 10 mw ERS unit in MSS-1 calculations than if its 10 mw ERS unit were excluded from MSS-1 treatment. CNO claims that these exhibits and conclusions are erroneous because they make incorrect assumptions.

CNO states that LPSC's first flaw is that it wrongly assumes that the unit has only three years of remaining service life if that unit is kept in service. CNO claims that L/M/MAG overlook the fact that the remaining life of a generating unit for cost depreciation purposes is not necessarily the same as that unit's remaining service life, which is defined as the remaining interval before the unit is worn-out and incapable of further use or operation in the future. CNO argues that L/M/MAG's second flaw is that they ignore certain costs associated with the hypothetical unit that its owner will continue to incur for so long as that unit is capable of use. CNO believes that such costs include property taxes, insurance, and ownership costs. Third, CNO argues that the unit owner is better-off under "Option 1-Keep in

Service" on Ex. No. LPSC-24 than under "Option 2 Place in ERS" because of the time value of money.

CNO claims that Staff's proposed remedy is excessively harsh under the facts of this case. CNO believes Staff's remedy lacks an appropriate design to ensure that its purpose of sanctioning Entergy management is accomplished. If any refunds are ordered, CNO proposes that the remedy be structured to protect AP&L and NOPSI ratepayers from having to absorb these refund amounts. CNO believes this can be accomplished by requiring a credit to the MSS-1 bills of LP&L and MP&L without the imposition of a corresponding debit to the MSS-1 bills of AP&L and NOPSI.

In its Reply Brief, CNO lists what it believes are the core principles to this proceeding, which support the finding that all of the Operating Companies, including LP&L and MP&L, bear the costs of the ERS units. First, CNO states that the purpose of MSS-1 is to share capacity costs among all of the Operating Companies on the Entergy System. Second, CNO claims that the ERS units were planned and constructed for the benefit of all of the Operating Companies. Third, the generating units which were placed in ERS status were among the generating units originally found by the FERC to have been planned and constructed for the benefit of the System as a whole and approved for cost-sharing by all of the Operating Companies under MSS-1. Fourth, all of the Operating Companies caused the costs of the ERS units to be incurred. Fifth, there are ongoing costs associated with the ERS units to the owners of those units. Sixth, the ERS units have provided, and continue to provide benefits to the entire Entergy System. Seventh, the ERS units already have been returned to service to meet the demands of the System as a whole, or are currently planned to be returned to service to meet the demands of the System as a whole. Finally, the Complainants themselves previously supported the inclusion

of the ERS units of AP&L, LP&L, MP&L and NOPSI in MSS-1 calculations.

APSC argues that no refunds are required by the equities of the case, nor would refunds further the purposes of the FPA. APSC contends that no party has proven that ratepayers suffered any harm, much less the millions of dollars now claimed by LPSC and MPSC. APSC states that a refund would unjustly shift the cost of generating capacity constructed for the benefit of the system as a whole. Furthermore, APSC believes that refunds would not place LP&L and MP&L in the same position they would have been in if ERS units had been excluded initially. Rather, APSC claims that refunds would more likely place LP&L and MP&L in a better position than they would have been in because they will have enjoyed all the benefits of an ERS program that would probably not have taken the same form. APSC I.B. at pp. 3-9.

APSC emphasizes that LPSC and MPSC have changed their positions since the merger hearing because they realized there may be a chance to recover refunds. According to APSC, during the merger case, witnesses for LPSC and MPSC stated that it was in the best interest of the existing EOCs and their ratepayers for the ERS units of the existing Operating Companies to continue to be counted in MSS-1 but for Gulf States' units to be excluded. *See* Tr. 118-19; Tr. 397. Both LPSC and MPSC now urge the Commission to exclude from MSS-1 calculations the very same ERS units they had previously recommended to be included, claiming that such a practice violates the System Agreement. As MPSC witness Dorman Davis admitted, MPSC decided to protest Entergy's practice of including the ERS units of the existing EOCs in MSS-1 only after MPSC realized that it might be able to acquire some monetary refunds as a result of the alleged violation. *See* Tr. 400-02. APSC claims that LPSC's motive is the same—if its new position is successful and its request for

retroactive refunds is granted, LP&L could receive a windfall of as much as $19.3 million.

APSC disputes L/M/MAG's claim that Entergy's actions resulted in "overpayments" by LP&L and a "loss of receipts" by MP&L, implying that LP&L and MP&L suffered financial harm as a result of the ERS program. APSC states that the parties fail to explain how this conclusion is reached. On the other hand, APSC emphasizes that the financial benefits realized by LP&L, MP&L and the other EOCs have been well established.

Ruling

In its Order Denying Complaint and Clarifying Earlier Order, with respect to retroactive refunds, the Commission directed:

> However, any decision in this case whether we will order retroactive refunds—and if so, who should be responsible (and in what proportion) for those refunds—is premature at this point. The Commission must first determine whether Entergy did, in fact, violate the System Agreement. If the judge ultimately concludes, based on his review of the record compiled in Docket No. EL94-13-000, that the answer to this question is yes, he should determine the dollar amount of such violation for the entire period that the violation occurred. We believe that the judge also should recommend an appropriate remedy. . . .

67 FERC ¶ 61,338, at p. 62,197.

In response to the Commission's direction, the ruling in Issue I above concluded that yes, Entergy did in fact violate the System Agreement. Accordingly, we must address what the appropriate remedy should be. In a section 206 proceeding, refunds usually are ordered prospectively from the date of the order instituting the proceedings. However, the

Commission, in its discretion, may order that refunds be made retroactively for the term of the violation. Should the Commission exercise that discretion in this proceeding? I believe the answer is no.

The application of MSS-1 treatment to ERS units has existed since the institution of the ERS program without complaint by any of the state regulatory bodies or any Entergy Operating Company. There is no evidentiary support for the proposition that Entergy knowingly violated the System Agreement. Neither the language of the System Agreement nor its application to ERS units were in any manner concealed from the Operating Companies or local regulatory bodies. There was no perception of a tariff violation until Staff witness Sammon first suggested so in his testimony in the Entergy/GSU merger proceeding in 1993.

At that time the concern was to protect the Operating Companies (and incidentally retail ratepayers) from any adverse effects of the proposed merger. LPSC and other parties proposed several conditions for Commission approval of the merger.

One of these conditions excluded existing Gulf States' ERS units from MSS-1 treatment. L/M/MAG claim that they did not focus on the application of MSS-1 at that time because it was not an issue in the merger proceeding. In formulating this condition, however, the parties must have been cognizant of the language and Entergy's application of the terms of Service Schedule MSS-1. While these facts do not excuse a tariff violation, they are indicative that all parties, including Entergy, were acting in good faith.

Prospective relief from a tariff violation is warranted but is retroactive retribution reasonable under these circumstances? I believe the answer is no.

Both Entergy and L/M/MAG refer to the Court of Appeals decision in *Towns of Concord, Norwood, & Wellesley v. FERC*, 955 F.2d 67 (D.C. Cir. 1992). This decision involved

the towns of Concord, Wellesley, and Norwood, Massachusetts, which demanded refunds of amounts paid to Boston Edison in violation of its FERC filed rate.[6] The Commission declined to order a refund of the amounts collected, and the Court of Appeals affirmed the Commission.

The court discussed the Federal Power Act and the filed rate doctrine in detail. It maintained that the principal issue in this case is "whether, in light of these provisions [sections 205(c) and 206(a) of the Federal Power Act] and the [filed rate] doctrine derived from them, the Commission has any discretion to withhold refunds when it discovers that a utility has imposed charges not in conformity with its rate schedules . . . ." The court found that "the Federal Power Act reveals no statutory command mandating refunds when the rate charged exceeds that filed." *Id.* at p. 72.

The court went on to say that there is no reason to suppose that the Commission's refusal to order a refund will undermine its primary jurisdiction over the reasonableness of rates, promote discriminatory rate payments, or in any other manner thwart the core purposes of the filed rate doctrine or of the statute. *Id.* at p. 75. Thus the Commission has discretion regarding whether to provide refunds so long as that decision is reasonable.

Because of the equitable aspects of refunds, the agency must show that it considered relevant factors and struck a reasonable accommodation among them. This is particularly so where retroactive refunds are sought in a section 206 proceeding. Hence, in the instant proceeding, several factors require consideration.

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[6] Specifically, the towns received most of their power requirements from Boston Edison. Boston Edison purchased some of its power from regional nuclear power companies. For thirteen years, those companies imposed certain charges relating to the storage and disposal of spent nuclear fuel on Boston Edison. Boston Edison passed these charges on to the towns, improperly, without prior approval from the FERC.

1. The Staff witness who raised the violation issue also found that despite an apparent violation, the end result was just, reasonable and non discriminatory. Despite the claims of L/M/MAG that costs were shifted from some Operating Companies to others, Staff's judgment in this regard is persuasive.

2. The Commission did not base its acceptance of the merger upon the condition eliminating Gulf States' ERS units from MSS-1 treatment. However the Commission did state that "we fully expect the Applicants to abide by their commitments made in this proceeding."

3. Entergy did not knowingly violate the edicts of the System Agreement. Entergy, together with the Operating Companies, believed they were complying with Service Schedule MSS-1.

Entergy does not deserve censure or punishment for its good faith actions. The only other purpose of ordering retroactive refunds would be to place the parties in *status quo*. This objective can not be obtained at this point in time. The L/M/MAG argument that permitting ERS units to remain in service rather than applying MSS-1 treatment would have been less expensive is not convincing. On the contrary, the evidence shows that keeping excess units in service would have required substantial expenditures. If there would have been no savings, why would L/M/MAG have consented to the MSS-1 treatment afforded to ERS units? CNO and APSC reasonably assert that their decisions to place excess generating units into ERS was predicated upon these units receiving MSS-1 treatment. Otherwise, there would be no reason to do so. Keeping excess generation in service would have been detrimental to all the Operating Companies and would have defeated the purposes of the ERS program.

The ERS program accomplished some important benefits for all of the Operating Companies. Allowing excess

generating units to be placed in ERS status promoted cost savings and efficiency. ERS status permits deferred maintenance and preserves the units as system reserves. There is evidence that ERS program resulted in operation and maintenance savings of $65 million. Ex. Nos. ENT-1 at p. 32; ENT-5. In addition, the availability of reserves avoids or delays the building of new generating capacity to meet expected load growth.

The Commission should not exercise its discretion to provide retroactive refunds.

Nor should the Commission order a refund of the time value of the principal. In *Western Resources*, the Commission explicitly revised its refund policy. Western Resources recovered "buy-down payments" through its wholesale fuel adjustment clause, without prior permission from the Commission. Prior to *Western Resources*, the Commission policy had been to require costs that a utility had improperly recovered to be refunded in full. In *Western Resources*, the utility had fully recovered all its costs prior to filing for a waiver with the Commission. The Commission concluded:

> On review of the case law . . . we have decided to change our policy. We will order Western to refund, with interest calculcated according to our regulations, 18 C.F.R. § 35.19a, the time value of the $500,000 between April 1, 1991 and January 7, 1993, the date it filed its Request for Waiver.

65 FERC at p. 62,251.

The Commission modified its previous policy. The Commission stated that had Western sought prior approval, the utility would have received permission to recover the buy-down payments through its wholesale fuel adjustment clause. *Id.* at p. 62,249. In *Western Resources*, the company clearly knew or should have known that prior approval was necessary. Thus in *Western Resources*, the Commission

propounded an appropriate penalty for good reason. In the instant proceeding, Entergy was not aware that a violation of the System Agreement was being committed and therefore did not file an application for a tariff amendment. Therefore, in the instant proceeding, such a penalty, as Staff advocates, would be harsh and is not warranted.

Issue III. Assuming a Violation of the System Agreement, What is the Dollar Amount of Such Violation for the Entire Period that the Violation Occurred?

L/M/MAG state that Entergy's violation of the System Agreement resulted in economic harm to two Operating Companies, LP&L and MP&L, and their ratepayers. L/M/MAG claim that the dollar amount of the economic harm from January 1, 1987, through 1993 is:

Company	*Refund (Payment)*	*Interest*	*Total*
AP&L.....	$(8,828,111)	$(6,895,697)	$(15,723,808)
LP&L.....	$11,252,905	$8,134,041	$19,386,946
MP&L.....	$10,845,744	$5,433,522	$16,279,266
NOPSI....	$(13,270,538)	$(6,671,866)	$(19,942,404)

See Ex. No. LPSC-5 at p. 1. L/M/MAG argue that this calculation captures the consequences of Entergy's violations through December 31, 1993, including an interest component based on the long companies' weighted cost of capital.

L/M/MAG describe how their calculations differ from Entergy's calculations in two respects. First, Entergy's calculation includes no interest. L/M/MAG argue that the recovery of interest is necessary to repair the harm caused and that the purpose of a refund should be to place the parties in the position they would have occupied absent the tariff violations. Second, Entergy's calculation uses an ERS begin date for the Lake Catherine Units 1 & 2 of January 1, 1991. LPSC witness Baron uses a beginning date of January 1, 1987 for those units. L/M/MAG state that AP&L's Lake Catherine

units were not "available" under the System Agreement as of December 31, 1986.

L/M/MAG also challenge Entergy's suggestion that if interest is allowed, the interest rate should be based upon 18 C.F.R. § 35.19, which requires interest to be calculated "at an average prime rate for calendar quarter on all excessive rates or charges," compounded quarterly. L/M/MAG state that 18 C.F.R. § 35.19 describes how to calculate refunds under suspension orders and this refund is based on the violation of a filed rate. L/M/MAG admits that while the C.F.R. method of calculating interest has been used by the FERC in the past, outside of the context of suspension orders, no rule or regulation requires its application.

Entergy claims that no refunds of any dollar amount are appropriate in this proceeding. For the record, however, Mr. Reagan retroactively recalculated the effect of excluding ERS units from past MSS-1 billings. The results of retroactively excluding the ERS units for the period ending December 31, 1993 are:

	Benefit	*Detriment*
AP&L		$6,295,577
LP&L	$10,604,007	
MP&L	$8,816,492	
NOPSI		$13,124,922
Total	$19,420,499	$19,420,499

Entergy I.B. at pp. 55-56. Entergy has not applied interest to these calculations because it believes interest is inappropriate for the same reasons such retroactive rate recalculations are inappropriate.

Entergy challenges L/M/MAG's calculation of interest using a "weighted cost of capital of the long companies—AP&L and MP&L—during each year 1987 through 1993."

Entergy believes that this approach for calculating interest is inconsistent with FERC's regulations and contrary to FERC precedent. Entergy argues that L/M/MAG fail to point to even one FERC case or other authority supporting their interest calculation proposal.

According to Entergy, L/M/MAG only argue that the interest they calculate is needed to "place the parties in the position they would have occupied" had the ERS units been excluded from MSS-1 calculation. Entergy claims that this argument lacks a factual basis. Entergy states that L/M/MAG failed to put forth any evidence that the Operating Companies in their jurisdiction incurred additional costs of debt because they lacked the amounts they claim should be refunded. This absence of any record evidence, according to Entergy, undermines any argument based on the "cost of capital." In addition, Entergy argues that it is impossible to place the parties in the position they would have been absent the implementation of the ERS program in its current form because the program would have been far different, or non-existent, if the ERS units were excluded from MSS-1 calculations.

Entergy also challenges L/M/MAG's claim that Entergy should be responsible for paying whatever additional interest amounts accrue between January 1, 1994 and the date refunds are made. Entergy believes this argument is untenable in light of Entergy's proposed Settlement. According to Entergy, the Settlement Offer clarifies that the Operating Committee has discretion to include ERS units in MSS-1. Entergy insists that because the Settlement Offer is effective January 1, 1994, the Settlement would obviate any claims of violation after the effective date.

Entergy claims that LPSC witness Baron erroneously treats Lake Catherine units 1 and 2 as entering ERS in 1986 because they were not being run. Entergy argues that many of its intermediate units rarely run at times of excess capacity

and those units are not on ERS. *See* Ex. No. CNO-1 at pp. 12-14. In order to place a unit in the ERS program, Entergy argues that two preliminary steps are necessary. First, candidate units must be selected for possible ERS status from a system-wide perspective. Second, the Operating Committee must approve each unit for inclusion in the ERS program. *See* Ex. No. ENT-14 at pp. 15-17. In absence of meeting those steps, Entergy insists that an idle unit simply remains an idle unit. Entergy states that the Lake Catherine units went into ERS in 1991. *See* Ex. No. ENT-20 at pp. 16-17.

Staff claims that the dollar amount of the violation, as calculated by Entergy, is $19,420,499. *See* Ex. Nos. ENT-20 at pp. 5-6; ENT-22. Staff argues that principal stops accruing as of December 31, 1993, however interest should continue to accrue on the principal.

CNO claims that no refunds should be imposed on rate-payers of NOPSI and AP&L. CNO opposes the LPSC's calculation of refund amounts, including the LPSC's attempt to add carrying charges based upon a weighted cost of capital. CNO states that even if carrying charges were appropriate, which they are not, FERC interest rates, which are based on the prime rate and compounded quarterly, must be used instead of the LPSC's proposed weighted cost of capital. *See* 18 C.F.R. § 35.19a.

CNO argues that it is particularly inequitable to award refunds and carrying charges sought by the LPSC from August 29, 1991, to the present. CNO claims that the LPSC knew of Entergy's practice of including ERS units in MSS-1 reserve equalization since at least August 29, 1991, yet did absolutely nothing to protest this treatment until 1994. CNO argues that those refunds and carrying charges are the product of LPSC's own inaction and unclean hands.

CNO states that even assuming it was equitable to order refunds of any of the principal or interest sought by

L/M/MAG, which it is not, the August 29, 1991 cut-off would at least mitigate the concurrent harm to AP&L and NOPSI resulting from an award of refunds in this proceeding. CNO claims that Ex. No. CNO-20 shows that amount of principal and interest, when calculated pursuant to the FERC's regulations and cut-off as of August 29, 1991, would be $8,549,804 to LP&L and $4,421,576 to MP&L. The total combined refund amount would be $12,971,380, compared with the $35.6 million sought by L/M/MAG. CNO R.B. at p. 32.

According to APSC, the total dollar effect of inclusion of ERS units in MSS-1 under Entergy wholesale rates is zero. APSC states that L/M/MAG have failed to prove that Entergy would have made the same decisions regarding which units to place in ERS if the Operating Committee had known that ERS generating units would be excluded from MSS-1 calculations. APSC argues that the record clearly shows that the same decisions would not have been made and refunds are not appropriate.

APSC claims that on an individual company basis, hypothetically, had the Operating Committee made the same decisions, and had the pre-merger ERS units been excluded from MSS-1 calculations, AP&L would have received $6,295,577 less; LP&L would have paid $10,604,007 less; MP&L would have received $8,816,492 more; and NOPSI would have paid $13,124,922 more. Ex. No. ENT-20 at p. 14. These are the same figures that Entergy uses.

APSC suggests that if refunds are ordered, the most equitable measure would be to offset the supposed harm by the uncontested, proven financial benefits that enured to all Entergy Operating Companies as a result of the ERS program. APSC believes that this approach would more accurately return the parties to the position they would have been had the Operating Committee known such an outcome would be the result of its implementation of an ERS program.

Under such an approach, APSC claims that LP&L's windfall of $10,604,007 would be offset by the approximate $15.5 million in savings realized to date, and MP&L's windfall of $8,816,492 would be reduced by the approximate $11.7 million in savings it has realized to date. Thus, as a matter of equity, APSC claims that neither LP&L nor MP&L are entitled to refunds in this instance.

Ruling

In its Order setting this matter for hearing, the Commission required the judge, if he finds that a violation occurred to "determine the dollar amount of such violation . . . and recommend an appropriate remedy." I have found that a violation did occur.

Pursuant to the Commission mandate, this section of the decision treats the monetary value of the violation. As discussed in Issue II above, this decision finds that retroactive refunds should not be ordered in this proceeding. Nevertheless, if refunds were an appropriate remedy, the proper dollar amount is discussed below.

L/M/MAG projects the money value of the violation including interest computed on the "weighted cost of capital." While L/M/MAG make an interesting argument, there is no support for this proposal either in Commission precedent or Commission regulations. There is no real controversy. The Commission regulation, set forth in 18 C.F.R. § 35.19a, provides for the appropriate rate of interest and controls this proceeding.

Entergy calculated the total amount of the violation to be $19,420,499. Staff agrees that Entergy's computation is correct. Although APSC vigorously insists that there was no violation and therefore the dollar amount should be zero, APSC agrees that if refunds are ordered, Entergy's computation is correct. CNO opposes any refund just as vigorously, yet suggests a cut-off date of August 29, 1991.

The violation, however, persisted throughout the pre-merger period ending with December 31, 1993.

L/M/MAG dispute Entergy's ERS begin date for Lake Catherine units 1 and 2. The record shows that Lake Catherine units 1 and 2 went into ERS on December 31, 1990. *See* Ex. No. ENT-23 at p. 1. The fact that these units were idle prior to that date is not conclusive evidence of a violation. L/M/MAG have not successfully refuted Entergy's claim that an idle unit must first meet the steps necessary for inclusion in the ERS program.

Thus if refunds were a suitable remedy, contrary to the finding in this decision, the appropriate dollar amount of the violation would be $19,420,499 with interest computed in accordance with 18 C.F.R. § 35.19a until refunds are made.

Issue IV. Should Service Schedule MSS-1 of the System Agreement be Amended Prospectively to Address Expressly the ERS Issue and if so, How?

Entergy, Staff, APSC and CNO have supported an Offer of Settlement designed to address post-merger treatment of ERS units under Service Schedule MSS-1.[7] The settlement language would prevent future disputes by amending the System Agreement to make it explicit that the Operating Committee is permitted to include in the MSS-1 calculations generating units that are placed into ERS status pursuant to specified factors.

Entergy believes that the settlement proposal should be adopted on two grounds. First, Entergy argues that it identifies an appropriate set of factors for reviewing the reasonableness of including ERS units. Second, Entergy claims that the proposal preserves the distribution of merger

[7] Ex. No. ENT-10 sets out a proposed Offer of Settlement that was not adopted.

benefits which the LPSC and other parties supported in the merger proceeding.

Entergy states that the proposed settlement language appropriately establishes relevant criteria for Operating Committee decision-making. Contrary to the position of L/M/MAG, Entergy believes the language is not ambiguous and does not create confusion. Entergy claims that although it vests the Operating Committee with discretion to apply the identified standards to the evolving needs of the Entergy System, it does not grant unfettered discretion. Rather, Entergy believes that the latitude given to the Operating Committee is tempered by reviewable parameters.

Entergy claims that there is no reason that a unit has to be on line and able to run on a minute-to-minute basis to count as "reserves" under Service Schedule MSS-1. Entergy states that MSS-1 equalizes reserves, and reserves include units that are kept back or stored up, and are not needed to meet daily operating conditions. Entergy argues that, as Mr. Sammon testified, the reserve equalization payments made among the Operating Companies under MSS-1 are simply part of the cost of enjoying life in the integrated Energy System. *See* Tr. 875. According to Entergy, so long as the ERS units are providing a benefit to the System, the owning companies should not lose MSS-1 credit for them.

Furthermore, all of the Operating Companies are equally responsible for the existence of excess capacity on the Entergy System. Entergy argues that it would be unduly discriminatory to include in MSS-1 some of the excess capacity owned by some Operating Companies, and penalize others by excluding the ERS units.

Staff's position is that Service Schedule MSS-1 should be amended to allow units of the original four Operating Companies in ERS to receive capacity credit in MSS-1. Staff

accepts the wording of the proposed settlement found in Ex. No. ENT-10 at pp. 4-5.

CNO believes that the System Agreement must be amended to clarify that the ERS units of AP&L, LP&L, MP&L, and NOPSI will be included in MSS-1 calculations. CNO supports the amendment to section 10.02(a) of Schedule MSS-1 as written in Ex. No. ENT-10 at pp. 4-5 and believes that it should be adopted prospectively.

APSC argues that Service Schedule MSS-1 should be amended prospectively, according to the language found in the Offer of Settlement dated February 16, 1994, to include ERS units in calculations for MSS-1. According to APSC, modifying the System Agreement to reflect the implementation of the ERS program, a program acknowledged by both the LPSC's and MPSC's witnesses as beneficial, will allow all EOCs to save money while ensuring that the Commission's well established policy of allocating the costs of generating capacity among all the EOCs continues.

APSC claims that if the pre-merger EOC's ERS units are excluded from MSS-1 calculations, a substantial portion of the projected merger-related benefits for the pre-merger EOCs will shift to Gulf States, primarily to the detriment of AP&L and NOPSI. APSC also argues that inclusion of ERS units in Service Schedule MSS-1 calculations will ensure that capacity costs incurred for the benefit of the Entergy System will continue to be equitably allocated among the EOCs.

APSC claims that placing units in ERS status reduces costs and provides economic benefit for the Entergy System. APSC states that despite the acknowledged benefits of the ERS program, LPSC and MPSC seek to shift the entire cost of the ERS program to the owning companies by excluding ERS units from MSS-1 calculations. APSC believes this attempt to retain the benefits of the ERS program and the ERS capacity, while avoiding the costs of that capacity, is nothing more than

a request for a discriminatory subsidization at the expense of AP&L and NOPSI, in violation of sections 205 and 206 of the Federal Power Act.

L/M/MAG oppose amending MSS-1 to address the ERS issue, because the existing MSS-1 language excludes ERS units by permitting only "available" units to be counted. A unit is "available" only to the extent the capability can be demonstrated and the unit is under the control of the System Operator or is down for maintenance or refueling. *See* Ex. No. ENT-2, at p. 32. L/M/MAG argue that ERS units are not "available" and should be excluded from the determination of company capability.

L/M/MAG believe that the proposed language should be rejected because it is ambiguous and provides the Operating Committee with unbridled discretion in administering the tariff. L/M/MAG claim the Entergy proposal does not explain how the factors to consider affect the determination of whether an ERS unit is available or unavailable. Furthermore, L/M/MAG believe that Entergy's proposed amendment basically allows Entergy to include anything in the MSS-1 tariff. They claim the settlement language allows the Operating Committee to do whatever it wants, so long as it considers the cited factors.

L/M/MAG also argue that the settlement proposal cannot be justified on the theory that it preserves an allocation of merger benefits. They claim that the FERC did not reallocate benefits in approving the merger. L/M/MAG argue that in any event, the requirement of payments under MSS-1 for capacity that provides no service would be an artificial "benefit" and not an allocation of true merger savings.

Staff opposes the proposal of LPSC witness Baron and MPSC witness Davis that ERS units owned by the four pre-merger Operating Companies should be excluded from MSS-1 computations prospectively. Staff believes that such an

exclusion would upset the allocation of benefits flowing to the post-merger Operating Companies which the Commission approved in Opinion No. 385, and is therefore unreasonable. *See* Ex. Nos. S-1, at pp. 9-10; S-4, at pp. 2-4. Staff agrees with Entergy witness Reagan's calculations of the allocation that such an exclusion would cause. Reagan estimates that during the period 1994-2003, Gulf States Utilities Company would benefit by $9,139,907 and MP&L would benefit by $242,879. The remaining Operating Companies would suffer detriments during the same period: AP&L $6,380,265; LP&L $236,265; and NOPSI $2,766,256. *See* Ex. Nos. ENT-20, at pp. 7, 21-22; ENT-25.

Ruling

Since the System Agreement was written before the ERS program was instituted, it does not adequately address the treatment of the ERS units. This failure is the cause of current controversy.

Staff and all parties, except L/M/MAG, proposed an amendment to section 10.02(a) of the System Agreement which was intended to eliminate the dispute over the application of MSS-1 treatment to ERS units. *See* appendix.

This decision has ruled that Entergy violated the System Agreement because it has included ERS units in MSS-1 when they were not considered "available" under the Agreement. The placement of ERS units in MSS-1 has been in existence for many years without complaint. Operating Companies have relied on including ERS units in MSS-1 when deciding whether or not to place units in ERS status. The ERS program has worked well, enhancing the efficiency of the System.

It is clear that the condition to exclude Gulf States' ERS units from MSS-1 in the merger proceeding, which was endorsed by L/M/MAG, did confer a substantial benefit to the existing Operating Companies. The contention that payments under MSS-1 for capacity is an artificial benefit is not warranted by the record. Units could and have been brought

back into service out of ERS as needed. The ability to do so, by delaying the necessity for construction of new generation facilities, is one clear benefit. Other benefits have been discussed previously in this decision.

The current wording of section 10.02 is problematic. Even though Staff witness was critical of the language, he found that including certain ERS units in MSS-1 was just and reasonable. The proposed amendment to section 10.02 cures the defects. The amendment is neither ambiguous nor does it provide the Operating Committee with unfettered discretion. The amendment sets out the parameters of the Operating Committee's discretion. The regulations of this Commission provide a remedy for any abuse of this discretion.

Service Schedule MSS-1 of the System Agreement should be amended prospectively. The language set forth in the appendix expressly addresses the ERS issue and is accepted.

Issue V. Assuming a Violation of the System Agreement, and Assuming that Refunds are an Appropriate Remedy, Who Should be Responsible (and in what Proportion) for those Refunds?

L/M/MAG argue that the bills should be recalculated and credits and charges assessed as if the tariff had been followed. They believe that Entergy should be required to pass the full amount of refunds, including interest, to LP&L and MP&L through a credit to future system bills. They also claim that Entergy should be allowed to surcharge the future system bills of AP&L and NOPSI for the benefit they received from the ERS violations, including interest. L/M/MAG assume this method parallels the one used by Entergy to correct accounting and other errors on System billings.

Entergy believes the issue in this proceeding regards wholesale costs and how those costs should be allocated among the Operating Companies to equalize the cost of reserve capacity on the Entergy system. Thus Entergy argues

that if LP&L and/or MP&L receives(s) a refund because it was allegedly overcharged, the other Operating Companies (AP&L and NOPSI) must have been undercharged. Entergy argues that the company and its shareholders are not supposed to be harmed in any way by this equalization process, which is a matter of cost allocation equity.

Entergy claims that the appropriate mechanism for providing a refund would be through revisions to the intra-system bill. Companies that allegedly overpaid would receive a credit; companies that underpaid would receive a corresponding debit. In this way the filed rate (the MSS-1 formula) does not change.

Staff's position is that Entergy should recompute the monthly bills to the Operating Companies for the period January 1, 1987 through December 31, 1994. Staff believes that refunds should be credited back to the time period in which an Operating Company experienced a deficit in billings. As an alternative, Staff believes credits could be applied against future MSS-1 billings. Staff states that the credits would be due to the Operating Company who received excessive MSS-1 billings.

According to Staff's proposal, based on computations of interest through October 14, 1994, AP&L would owe payments of $3,006,967 and NOPSI would owe payments of $4,180,228. *See* Tr. 866; Tr. 858. Staff calculates that LP&L would receive credits of $4,811,774 and MP&L would receive credits of $2,375,421. Staff I.B. at pp. 25-26.

CNO argues that shareholders must be held responsible for any refunds. CNO believes that fairness requires protecting ratepayers from having to absorb the costs of any refunds. CNO claims that the purpose of the remedy ought to be determinative of its design and in this case, the purpose is to sanction Entergy management for negligently failing to adhere to its filed rate and to deter potential tariff violations

in the future. CNO maintains that the Commission cannot allow Entergy, or any company, to shift costs to ratepayers incurred as a result of its negligent or imprudent decision-making. CNO cites both Supreme Court and FERC decisions to support its theory.

CNO states that Entergy can credit the MSS-1 bills of LP&L and MP&L for any refund amounts without a corresponding debit to the MSS-1 bills of NOPSI and AP&L. CNO argues against the assertion that the wholesale rate at issue must always be a zero sum game. CNO asserts that MSS-1 does not have to be a zero sum game when it comes to fashioning an equitable refund remedy.

CNO also suggests that in the alternative, the Commission could direct its Staff to seek civil penalties against Entergy management in accordance with sections 314, 315, 316 and 317 of the FPA. CNO R.B. at p. 39 (citing 16 U.S.C. §§ 825m, 825n, 825o, 825p). CNO claims that the purpose of FERC Staff's proposed refund remedy is to sanction Entergy management for violating its filed tariff. *See* Ex. No. S-4 at pp. 7-8. CNO believes that a sanction under the civil penalty procedures would be more equitable to Entergy management and commensurate with the type of technical violation that allegedly occurred.

APSC argues that any refunds, if ordered, should not be borne by retail ratepayers.

APSC challenges Entergy's proposal that refunds should not be borne by shareholders. APSC argues, since MSS-1 at the wholesale level is a "zero-sum game," Entergy's recommendation is premised on the assumption that refunds will be flowed through at retail by LP&L and MP&L, thus necessitating a corresponding recovery at retail by AP&L and NOPSI. APSC claims that Entergy's argument violates two basic rate-making principles: (1) the doctrine against retroactive rate-making; and (2) the principle that a utility is entitled to rates which allow it the opportunity to earn its

reasonable cost of service including a return on investment, but no more.

APSC asserts that Entergy has failed to show that shareholders even need to be "made whole," since it has failed to prove that, if refunds are ordered Entergy will not have recovered its cost of service during the refund period. APSC believes that allowing Entergy to recover from ratepayers any refunds ordered would be piecemeal rate-making. This would result in ratepayers being unfairly assessed for an under-recovery of only this one particular revenue component, without a review of all other cost or revenue changes. APSC claims that absent a showing by Entergy of an overall under-recovery of the costs of service during the 1987-1994 period, Entergy's proposal that ratepayers bear the burden of any refunds should be rejected.

Entergy argues that this is strictly a wholesale contract matter, and the Commission should only consider the effect of its decision on the wholesale level. Entergy claims that CNO provided no basis for holding shareholders responsible for refunds. Entergy asserts that neither negligence or imprudence is an issue in this case because Entergy acted to save costs and reduce rates to all Operating Companies. Furthermore, Entergy challenges the cases relied on by CNO.

Ruling

Assuming a violation of the System Agreement, and assuming that refunds are an appropriate remedy, the bills should be recalculated and credits and charges assessed to the Operating Companies as if the tariff had been followed. This remedy properly allocates overpayments and underpayments among the Operating Companies. This remedy would put the parties in the position they would have been in had the System Agreement not been violated.

CNO claims that if refunds are ordered, Entergy shareholders should be responsible for the amounts assessed. CNO

sponsors a remedy to sanction Entergy for negligently failing to adhere to its filed rate and to deter potential tariff violations in the future. CNO argues that an equitable refund remedy need not result in a "zero sum" game. CNO's proposal to credit to certain bills without a corresponding debit to other bills results in Entergy shareholders bearing the costs of the violation. The CNO proposal is not appropriate.

The cases cited by CNO deal with issues of imprudence, negligence, mismanagement, or inefficiency. None of these issues are present here. Entergy's violation was not due to imprudence, negligence, mismanagement or inefficiency. As discussed throughout this decision, Entergy acted in good faith. Actions made in good faith do not deserve sanction and are not in need of deterrence.

Entergy's proposal for handling refunds appears fair and reasonable and is reasonable. Under this proposal, each Operating Company would receive or owe credits in the proportions that they received or paid compensation under MSS-1 for the appropriate period.

Conclusion

Again, it is emphasized that this decision finds that retroactive refunds should not be ordered. The appropriate remedy is the adoption of the proposed amendment to the System Agreement set forth in the appendix.

Order

It is ORDERED, subject to review by the Commission on exceptions or on its own motion, as provided in the Commission's Rules of Practice and Procedure, that within 30 days of the issuance of the Final Order of the Commission adopting the Initial Decision in this proceeding, all parties shall take the appropriate action to implement all the rulings made in this decision.

Appendix

Offer of Settlement EL94-13-000

Settlement Provisions

Section 10.02(a) of the System Agreement shall be clarified to explicitly state that a unit that is placed in ERS with the intent of returning the unit to service at a future date in order to meet Entergy System requirements may be considered available for purposes of calculating reserve equalization payments under MSS-1. The amendment is shown below in ***bold type and underlined*** and is set out in the context of section 10.02(a). The language shown in *italics* is proposed to be added (along with another provision) to this section of the System Agreement by a Compliance Filing submitted to the Commission on December 30, 1993, in the merger proceedings, Docket Nos. EC92-21-000 and ER92-806-000. Section 10.02(a) shall read as follows:

> The total capability of available generating units owned, operated under Operating Agreements for its own benefit, or leased by such Company, which units shall be included at their demonstrated net output measured in megawatts under conditions established by the Operating Committee. A unit is considered available to the extent the capability can be demonstrated and (1) is under the control of the System Operator, or (2) is down for maintenance or nuclear refueling, *or (3) is in extended reserve shutdown (ERS) with the intent of returning the unit to service at a future date in order to meet Entergy System requirements. The Operating Committee's decision to consider an ERS unit to be available to meet future System requirements shall be evidenced in the minutes of the Operating Committee and shall be based on consideration of current and future resource needs, the projected length of time the unit would be in ERS*

status, the projected cost of maintaining such unit, and the projected cost of returning the unit to service. A unit, *including an* ERS unit, is considered unavailable if in the judgment of the Operating Committee it is of insufficient value in supplying system loads because of (1) obsolescence, (2) physical condition (3) reliability, (4) operating cost, (5) start-up time required, or (6) lack of due-diligence in effecting repairs or nuclear refueling in the event of a scheduled or unscheduled outage. *Notwithstanding the foregoing*, the generating units of Gulf States that were in extended reserve shutdown on the date of the merger of Entergy and Gulf States, shall not be considered available for the purpose of determining Gulf States' Capability in the Service Schedule MSS-1 Reserve Equalization calculation until the units are brought into service.

APPENDIX F

SUPREME COURT OF LOUISIANA

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From: CLERK OF THE SUPREME COURT OF LOUISIANA

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On the 24th day of May, 2002, the following action was taken by the Supreme Court of Louisiana in the case(s) listed below:

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Rehearing(s) Denied:

2001-CA-1725 ENTERGY LOUISIANA, INC. V. LOUISIANA PUBLIC SERVICE COMMISSION, ET AL. (Parish of E. Baton Rouge)
KIMBALL, J., would grant a rehearing.
TRAYLOR, J., would grant a rehearing.

APPENDIX G

Entergy Services, Inc. and Gulf States Utilities Company,
Docket No. EL94-13-002

Order Denying Rehearing
(Issued February 3, 1998)

Before Commissioners: James J. Hoecker, Chairman; Vicky A. Bailey, William L. Massey, and Linda Breathitt.

[Opinion No. 415-A Text]

I. Background

In Opinion No. 415,[1] the Commission affirmed an Initial Decision finding, *inter alia*, that: (1) the Entergy Operating Companies had violated the Entergy System Agreement (System Agreement) by including generating units in extended reserve shutdown (ERS)[2] under the System Agreement's Service Schedule MSS-1 (MSS-1), Reserve Equalization;[3] (2) based on a balancing of the pertinent equities, refunds were not appropriate; and (3) the System Agreement should

[1] *Entergy Services, Inc. and Gulf States Utilities Company*, Opinion No. 415, 80 FERC ¶ 61,197 (1997).

[2] As explained in Opinion No. 415, the ERS program allows the Entergy Operating Companies to place generating units in an inactive status and thereby reduce operating staff, maintenance costs, and defer the costs of repairing units. By deferring maintenance of units and yet preserving units as system reserves, the ERS program has allowed the Entergy Corporation (Entergy) system to lower its costs and also obviated the need to build new capacity. Entergy has estimated that, through August 31, 1994, the ERS program produced net savings of more than $65 million for its system. *See* Ex. ENT-1 at 32.

[3] Service Schedule MSS-1, set forth in section 10 of the System Agreement, provides the mechanism for equalizing system reserves among the Entergy Operating Companies.

be amended prospectively to clarify under what circumstances ERS units should be included in the Schedule MSS-1 calculation.

On September 4, 1997, the Louisiana Public Service Commission, the Mississippi Public Service Commission, and the State of Mississippi (collectively, State Agencies) filed a request for rehearing of Opinion No. 415. State Agencies claim that the Commission erred in Opinion No. 415 by: (1) not ordering a full refund, with interest, to remedy the violation of the System Agreement; (2) finding that Entergy and its shareholders did not benefit as a result of the ERS program; (3) finding that the benefits of the ERS program were enjoyed by customers of Louisiana Power & Light Company (LP&L) and Mississippi Power & Light Company (MP&L) and that the inability to include ERS units in Schedule MSS-1 calculations would provide a disincentive to participate in the ERS program; (4) approving the amendment to the System Agreement; and (5) failing to quantify damages to reflect the ineligible Schedule MSS-1 inclusion, plus interest.

II. Discussion

We deny State Agencies' request for rehearing. While State Agencies correctly point out that the Commission's general policy is to order refunds to remedy overcharges,[4] in this case the equities support denial of State Agencies' refund request. Even though there was a violation of the System Agreement, the Commission found that the end result of the treatment of the ERS units was just, reasonable, and not unduly discriminatory. As a result, we did not believe that the violation of the System Agreement resulted in overcharges that would, on balance, justify imposition of refunds.[5] We

[4] Rehearing at 4.

[5] State Agencies' incorrectly argue that our denial of refunds abdicates our responsibility to afford parties protection against a violation of a

found in Opinion No. 415 that the only appropriate remedy in this case is to amend the System Agreement prospectively to provide clarity in determining when ERS units should be included in Schedule MSS-1. Nothing raised in State Agencies' rehearing changes these conclusions.

State Agencies argue that the Commission erred in its balancing of the equities in Opinion No. 415. Specifically, State Agencies claim that Entergy misallocated Schedule MSS-1 costs for purposes of benefitting its shareholders and that the ERS savings did not flow through to ratepayers because Entergy pursued a policy of avoiding rate cases.[6] State Agencies also maintain that the Commission improperly concluded that Schedule MSS-1 treatment was necessary to provide proper incentives for the Entergy Operating Companies to participate in the ERS program.[7]

State Agencies have not adequately supported their claims. The record evidence cited by State Agencies (*e.g.*, Tr. 587-591) does not show that Entergy avoided rate cases so that its shareholders could retain the cost savings from the ERS program; rather, the record indicates that, by cutting costs, Entergy was able to avoid *rate increase* filings. This was certainly beneficial to ratepayers. Moreover, as pointed out by a Commission trial staff witness at hearing, given that only one of the Entergy Operating Companies, *i.e.*, Arkansas Power & Light Company (AP&L), has wholesale customers, and that most of AP&L's wholesale customers are served pursuant to cost-of-service formula rates, most of those

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formula rate. Rehearing at 7-9. This section 206 proceeding has provided State Agencies with the necessary forum to challenge the Entergy Operating Companies' implementation of the formula rate. In these circumstances, however, the record demonstrates that the ordering of refunds is not appropriate.

[6] Rehearing at 10-13.

[7] *Id.* at 13-22.

customers should have received their share of ERS savings.[8] To the extent State Agencies believed that an individual Operating Company was overcollecting costs prior to this proceeding, they were free to file a complaint under section 206 of the Federal Power Act challenging the overall level of such rates or the charges assessed under the System Agreement to that individual Operating Company,[9] but they did not do so.

The equitable factors referenced in Opinion No. 415 demonstrate that it was appropriate not to require refunds in these circumstances.[10] Moreover, as was explained in Opinion No. 415, the ERS units had been accorded Schedule MSS-1 treatment prior to being placed in ERS status, and it is

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[8] Ex. S-4 at 11-12. Retail customers benefitted from the ERS program because: (1) the program enabled the Entergy system to postpone construction and acquisition of new facilities to meet load growth; (2) the program led to a reduction in the rates for Schedule MSS-3 economy energy sales; and (3) there was an opportunity for ERS cost savings to be passed through in LP&L's retail rate case filed after the inception of the program. *See* Ex. S-4 at 11-13; Ex. ENT-1 at 34, 48-51, 59-60, 74; Ex. ENT-20 at 6, 19-21; Ex. ENT-34 at 7-11; Ex. ENT-14 at 30; Ex. LPSC-8 at 2-3, 9.

[9] The hypothetical examples set forth in the tables presented by State Agencies, attempting to depict that Schedule MSS-1 treatment of ERS units permits overcollecting of costs, are based on incorrect assumptions and fail to account for significant costs. *See* Rehearing at 16-18. The tables fail to recognize that, if an Operating Company were to place a unit in ERS status and temporarily forego Schedule MSS-1 recovery, it would continue to incur significant costs associated with that ERS unit, *e.g.*, capital costs, property taxes, and insurance (*see* Tr. 947-48 and Ex. ENT-1 at 41), that it would not be recovering. Significantly, the tables also fail to account for the time value of money, because they do not reflect the fact that revenue received during early years of the study period is more valuable on a net present value basis than the same revenue received during later years of the study period. *See* New Orleans City Council Brief Opposing Exceptions at 34-35; Entergy Reply Brief at 21-22; Entergy Brief Opposing Exceptions at 62-63.

[10] 80 FERC at pp. 61,787-88.

uncontroverted that these units would have continued to be eligible for Schedule MSS-1 treatment had Entergy not implemented the ERS program. Thus, contrary to State Agencies' contentions, to require the discontinuation of Schedule MSS-1 inclusion once a unit was placed in ERS status would have created a disincentive for the Entergy Operating Companies to place units in ERS status.[11] Continuation of Schedule MSS-1 treatment should not be denied in circumstances where an Entergy Operating Company seeks to reduce costs by participating in the ERS program.

Finally, we reject State Agencies' arguments that we erred in approving the amendment to the System Agreement and in failing to quantify damages. As noted in Opinion No. 415, this proceeding arose because section 10.02 of the System Agreement failed to encompass the ERS program. The amendment accepted in Opinion No. 415 cures this defect by defining the parameters that the Entergy Operating Committee must follow in determining whether a unit is eligible for inclusion in Schedule MSS-1. With respect to the refund issue, since we have found that refunds are not appropriate in this proceeding, there was and is no need to quantify damages.

The Commission orders:

State Agencies' request for rehearing is hereby denied.

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[11] *See* Tr. at 655-56; Ex. S-4 at 6; Ex. ENT-1 at 40-41; Ex. ENT-14 at 41 ("If MSS-1 impacts were a factor in an Operating Company's decision to put a candidate unit into ERS status, the rate and cost impacts of exclusion from MSS-1 may have discouraged Operating Company participation in the ERS program.").

APPENDIX H

CONSTITUTIONAL PROVISIONS

The Commerce Clause (U.S. Const. art. I, § 8, cl. 3):

> The Congress shall have Power . . . To regulate Commerce with foreign Nations, and among the several States and with the Indian Tribes . . . .

The Supremacy Clause (U.S. Const. art. VI, cl. 2):

> This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the Contrary notwithstanding.

APPENDIX I

STATUTES

16 U.S.C. § 824:

Declaration of policy; application of subchapter

(a) Federal regulation of transmission and sale of electric energy

It is declared that the business of transmitting and selling electric energy for ultimate distribution to the public is affected with a public interest, and that Federal regulation of matters relating to generation to the extent provided in this subchapter and subchapter III of this chapter and of that part of such business which consists of the transmission of electric energy in interstate commerce and the sale of such energy at wholesale in interstate commerce is necessary in the public interest, such Federal regulation, however, to extend only to those matters which are not subject to regulation by the States.

(b) Use or sale of electric energy in interstate commerce

(1) The provisions of this subchapter shall apply to the transmission of electric energy in interstate commerce and to the sale of electric energy at wholesale in interstate commerce, but except as provided in paragraph (2) shall not apply to any other sale of electric energy or deprive a State or State commission of its lawful authority now exercised over the exportation of hydroelectric energy which is transmitted across a State line. The Commission shall have jurisdiction over all facilities for such transmission or sale of electric energy, but shall not have jurisdiction, except as specifically provided in this subchapter and subchapter III of this chapter, over facilities used for the generation of electric energy or over facilities used in local distribution or only for the transmission of electric energy in intrastate commerce, or over facilities for the transmission of electric energy consumed wholly by the transmitter.

* * *

(c) Electric energy in interstate commerce

For the purpose of this subchapter, electric energy shall be held to be transmitted in interstate commerce if transmitted from a State and consumed at any point outside thereof; but only insofar as such transmission takes place within the United States.

(d) "Sale of electric energy at wholesale" defined

The term "sale of electric energy at wholesale" when used in this subchapter, means a sale of electric energy to any person for resale.

(e) "Public utility" defined

The term "public utility" when used in this subchapter and subchapter III of this chapter means any person who owns or operates facilities subject to the jurisdiction of the Commission under this subchapter (other than facilities subject to such jurisdiction solely by reason of section 824i, 824j, or 824k of this title).

* * *

(June 10, 1920, c. 285, § 201, as added Aug. 26, 1935, c. 687, Title II, § 213, 49 Stat. 847, and amended Nov. 9, 1978, Pub.L. 95-617, Title II, § 204(b), 92 Stat. 3140; Oct. 24, 1992, Pub.L. 102-486, Title VII, § 714, 106 Stat. 2911.)

16 U.S.C. § 824d:

Rates and charges; schedules; suspension of new rates; automatic adjustment clauses

(a) Just and reasonable rates

All rates and charges made, demanded, or received by any public utility for or in connection with the transmission or sale of electric energy subject to the jurisdiction of the Commission, and all rules and regulations affecting or per-

taining to such rates or charges shall be just and reasonable, and any such rate or charge that is not just and reasonable is hereby declared to be unlawful.

(b) Preference or advantage unlawful

No public utility shall, with respect to any transmission or sale subject to the jurisdiction of the Commission, (1) make or grant any undue preference or advantage to any person or subject any person to any undue prejudice or disadvantage, or (2) maintain any unreasonable difference in rates, charges, service, facilities, or in any other respect, either as between localities or as between classes of service.

(c) Schedules

Under such rules and regulations as the Commission may prescribe, every public utility shall file with the Commission, within such time and in such form as the Commission may designate, and shall keep open in convenient form and place for public inspection schedules showing all rates and charges for any transmission or sale subject to the jurisdiction of the Commission, and the classifications, practices, and regulations affecting such rates and charges, together with all contracts which in any manner affect or relate to such rates, charges, classifications, and services.

(d) Notice required for rate changes

Unless the Commission otherwise orders, no change shall be made by any public utility in any such rate, charge, classification, or service, or in any rule, regulation, or contract relating thereto, except after sixty days' notice to the Commission and to the public. Such notice shall be given by filing with the Commission and keeping open for public inspection new schedules stating plainly the change or changes to be made in the schedule or schedules then in force and the time when the change or changes will go into effect. The Commission, for good cause shown, may allow changes

to take effect without requiring the sixty days' notice herein provided for by an order specifying the changes so to be made and the time when they shall take effect and the manner in which they shall be filed and published.

(e) Suspension of new rates; hearings; five-month period

Whenever any such new schedule is filed the Commission shall have authority, either upon complaint or upon its own initiative without complaint, at once, and, if it so orders, without answer or formal pleading by the public utility, but upon reasonable notice, to enter upon a hearing concerning the lawfulness of such rate, charge, classification, or service; and, pending such hearing and the decision thereon, the Commission, upon filing with such schedules and delivering to the public utility affected thereby a statement in writing of its reasons for such suspension, may suspend the operation of such schedule and defer the use of such rate, charge, classification, or service, but not for a longer period than five months beyond the time when it would otherwise go into effect; and after full hearings, either completed before or after the rate, charge, classification, or service goes into effect, the Commission may make such orders with reference thereto as would be proper in a proceeding initiated after it had become effective. If the proceeding has not been concluded and an order made at the expiration of such five months, the proposed change of rate, charge, classification, or service shall go into effect at the end of such period, but in case of a proposed increased rate or charge, the Commission may by order require the interested public utility or public utilities to keep accurate account in detail of all amounts received by reason of such increase, specifying by whom and in whose behalf such amounts are paid, and upon completion of the hearing and decision may by further order require such public utility or public utilities to refund, with interest, to the persons in whose behalf such amounts were paid, such portion of such increased rates or charges as by its decision

shall be found not justified. At any hearing involving a rate or charge sought to be increased, the burden of proof to show that the increased rate or charge is just and reasonable shall be upon the public utility, and the Commission shall give to the hearing and decision of such questions preference over other questions pending before it and decide the same as speedily as possible.

(f) Review of automatic adjustment clauses and public utility practices; action by Commission; "automatic adjustment clause" defined

(1) Not later than 2 years after November 9, 1978, and not less often than every 4 years thereafter, the Commission shall make a thorough review of automatic adjustment clauses in public utility rate schedules to examine—

(A) whether or not each such clause effectively provides incentives for efficient use of resources (including economical purchase and use of fuel and electric energy), and

(B) whether any such clause reflects any costs other than costs which are—

(i) subject to periodic fluctuations and

(ii) not susceptible to precise determinations in rate cases prior to the time such costs are incurred.

Such review may take place in individual rate proceedings or in generic or other separate proceedings applicable to one or more utilities.

(2) Not less frequently than every 2 years, in rate proceedings or in generic or other separate proceedings, the Commission shall review, with respect to each public utility, practices under any automatic adjustment clauses of such

utility to insure efficient use of resources (including economical purchase and use of fuel and electric energy) under such clauses.

(3) The Commission may, on its own motion or upon complaint, after an opportunity for an evidentiary hearing, order a public utility to—

(A) modify the terms and provisions of any automatic adjustment clause, or

(B) cease any practice in connection with the clause,

if such clause or practice does not result in the economical purchase and use of fuel, electric energy, or other items, the cost of which is included in any rate schedule under an automatic adjustment clause.

(4) As used in this subsection, the term "automatic adjustment clause" means a provision of a rate schedule which provides for increases or decreases (or both), without prior hearing, in rates reflecting increases or decreases (or both) in costs incurred by an electric utility. Such term does not include any rate which takes effect subject to refund and subject to a later determination of the appropriate amount of such rate.

(June 10, 1920, c. 285, § 205, as added Aug. 26, 1935, c. 687, Title II, § 213, 49 Stat. 851, and amended Nov. 9, 1978, Pub.L. 95-617, Title II, §§ 207(a), 208, 92 Stat. 3142.)

16 U.S.C. § 824e.

Power of Commission to fix rates and charges; determination of cost of production or transmission

(a) Unjust or preferential rates, etc.; statement of reasons for changes; hearing; specification of issues

Whenever the Commission, after a hearing had upon its own motion or upon complaint, shall find that any rate, charge, or classification, demanded, observed, charged, or

collected by any public utility for any transmission or sale subject to the jurisdiction of the Commission, or that any rule, regulation, practice, or contract affecting such rate, charge, or classification is unjust, unreasonable, unduly discriminatory or preferential, the Commission shall determine the just and reasonable rate, charge, classification, rule, regulation, practice, or contract to be thereafter observed and in force, and shall fix the same by order. Any complaint or motion of the Commission to initiate a proceeding under this section shall state the change or changes to be made in the rate, charge, classification, rule, regulation, practice, or contract then in force, and the reasons for any proposed change or changes therein. If, after review of any motion or complaint and answer, the Commission shall decide to hold a hearing, it shall fix by order the time and place of such hearing and shall specify the issues to be adjudicated.

(b) Refund effective date; preferential proceedings; statement of reasons for delay; burden of proof; scope of refund order; refund orders in cases of dilatory behavior; interest

Whenever the Commission institutes a proceeding under this section, the Commission shall establish a refund effective date. In the case of a proceeding instituted on complaint, the refund effective date shall not be earlier than the date 60 days after the filing of such complaint nor later than 5 months after the expiration of such 60-day period. In the case of a proceeding instituted by the Commission on its own motion, the refund effective date shall not be earlier than the date 60 days after the publication by the Commission of notice of its intention to initiate such proceeding nor later than 5 months after the expiration of such 60-day period. Upon institution of a proceeding under this section, the Commission shall give to the decision of such proceeding the same preference as provided under section 824d of this title and otherwise act as speedily as possible. If no final decision is rendered by the

refund effective date or by the conclusion of the 180-day period commencing upon initiation of a proceeding pursuant to this section, whichever is earlier, the Commission shall state the reasons why it has failed to do so and shall state its best estimate as to when it reasonably expects to make such decision. In any proceeding under this section, the burden of proof to show that any rate, charge, classification, rule, regulation, practice, or contract is unjust, unreasonable, unduly discriminatory, or preferential shall be upon the Commission or the complainant. At the conclusion of any proceeding under this section, the Commission may order the public utility to make refunds of any amounts paid, for the period subsequent to the refund effective date through a date fifteen months after such refund effective date, in excess of those which would have been paid under the just and reasonable rate, charge, classification, rule, regulation, practice, or contract which the Commission orders to be thereafter observed and in force: *Provided*, That if the proceeding is not concluded within fifteen months after the refund effective date and if the Commission determines at the conclusion of the proceeding that the proceeding was not resolved within the fifteen-month period primarily because of dilatory behavior by the public utility, the Commission may order refunds of any or all amounts paid for the period subsequent to the refund effective date and prior to the conclusion of the proceeding. The refunds shall be made, with interest, to those persons who have paid those rates or charges which are the subject of the proceeding.

(c) Refund considerations; shifting costs; reduction in revenues; "electric utility companies" and "registered holding company" defined

Notwithstanding subsection (b) of this section, in a proceeding commenced under this section involving two or more electric utility companies of a registered holding company, refunds which might otherwise be payable under subsection

(b) of this section shall not be ordered to the extent that such refunds would result from any portion of a Commission order that (1) requires a decrease in system production or transmission costs to be paid by one or more of such electric companies; and (2) is based upon a determination that the amount of such decrease should be paid through an increase in the costs to be paid by other electric utility companies of such registered holding company: *Provided*, That refunds, in whole or in part, may be ordered by the Commission if it determines that the registered holding company would not experience any reduction in revenues which results from an inability of an electric utility company of the holding company to recover such increase in costs for the period between the refund effective date and the effective date of the Commission's order. For purposes of this subsection, the terms "electric utility companies" and "registered holding company" shall have the same meanings as provided in the Public Utility Holding Company Act of 1935, as amended [15 U.S.C.A. § 79 et seq.].

(d) Investigation of costs

The Commission upon its own motion, or upon the request of any State commission whenever it can do so without prejudice to the efficient and proper conduct of its affairs, may investigate and determine the cost of the production or transmission of electric energy by means of facilities under the jurisdiction of the Commission in cases where the Commission has no authority to establish a rate governing the sale of such energy.

(June 10, 1920, c. 285, § 206, as added Aug. 26, 1935, c. 687, Title II, § 213, 49 Stat. 852, and amended Oct. 6, 1988, Pub.L. 100-473, § 2, 102 Stat. 2299.)

16 U.S.C. § 825e.

Any person, State, municipality, or State commission complaining of anything done or omitted to be done by any licensee or public utility in contravention of the provisions of this chapter may apply to the Commission by petition which shall briefly state the facts, whereupon a statement of the complaint thus made shall be forwarded by the Commission to such licensee or public utility, who shall be called upon to satisfy the complaint or to answer the same in writing within a reasonable time to be specified by the Commission. If such licensee or public utility shall not satisfy the complaint within the time specified or there shall appear to be any reasonable ground for investigating such complaint, it shall be the duty of the Commission to investigate the matters complained of in such manner and by such means as it shall find proper.

(June 10, 1920, c. 285, § 306, as added Aug. 26, 1935, c. 687, Title II, § 213, 49 Stat. 856.)